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Working Capital Management of Hotel Industry in India: An Analysis

Dr. Sanjeev Bansal* **& Dr. Dimple Khosla****

*Professor, Department Of Economics, Kurukshetra University, Kurukshetra, India
**Assistant Professor, Dept. Of Commerce, Dyal Singh College, Karnal, India

Abstract

There is a lot of potential for growth of hospitality and tourism industry in India and abroad due to worldwide industrial development, increased earnings of individuals, economic growth of tourists producing nations, improved transport and communication means etc. Further, India hosted Commonwealth Games in 2010 and co-hosted the Cricket World Cup in 2011 and has multiple plans to promote yoga and meditation, rural tourism, sports tourism, medical tourism, adventure tourism etc. Thus, the future of Indian hospitality and tourism industry seems to be very positive. But, the hotel industry in India is facing a number of problems such as low occupancy rate, increasing competition, high taxes, increasing cost, fuel shortage and so forth. All these affect the profitability of the hotel industry adversely. Most of these problems are uncontrollable. Thus, it is necessary for the Indian hotel industry to manage its available resources optimally to enhance the profitability as the management of working capital and fixed assets affect the profitability of a business to a large extent. Thus, it is necessary for the hoteliers to manage their working capital efficiently. The main aim of the paper is to know whether hoteliers are succeeded in managing their working capital efficiently or not.

TOURISM AND HOTEL INDUSTRY IN INDIA

In recent years, Indian tourism and hospitality industry has emerged as one of the fastest growing industries in terms of capital invested, foreign exchange earnings and employment generation. It helps the developing countries like India in generating foreign exchange earnings and resolving the problem of employment of its ever-growing population as it is considered as highly labour intensive service industry, where the employment-investment ratio is higher than any other industry. Travel and tourism directly creates employment opportunities in hotels, restaurants, airlines, travel agencies, passenger ships, and as a result of the spread effect creates jobs in industries like construction, telecommunication, manufacturing and the retail trader.

Due to phenomenal increase in tourism activities, the hotel business has grown beyond expectations at national as well as international level. At present about 789 million tourists are crossing international boarder every year and they are spending nearly 685 billion US Dollars. This figure was just 100 million in 1964. The figure is likely to swell to 1.5 billion by 2015 and 2 billion by 2020 as per projection by world tourism organisation. International tourists here in India were 6.57 million in 2011 as against 4.78 million tourists in

2010. Foreign exchange earnings from these tourists were about 33000 crores of rupees in 2011 as against Rs.21429 crores in 2010. It is expected that this growth will continue during the next couple of years if no adverse incident happens in India or the South East Region. According to an estimate of CII, the number of foreign tourists visiting India is likely to increase to 50 million by 2020. As per estimates of Ministry of Tourism, 1,50,000 hotel rooms of different categories are required to be added to the existing available rooms in the next couple of years to accommodate all the foreign tourists and this will involve an investment of Rs. 35,000 crores. Obviously, there is a good scope for hotel business all over the world including India and these estimates will boost hotel business in India.

The hotel industry in India is facing a number of problems such as low occupancy rate, increasing competition, high taxes, increasing cost, fuel shortage and so forth. All these affect the profitability of the hotel industry adversely. Most of these problems are uncontrollable. Thus, it is necessary for the Indian hotel industry to manage its available resources (current as well as fixed assets) optimally to enhance the profitability as the management of working capital and fixed assets affect the profitability of a business to a large extent. There is a lot of potential for growth of hospitality and tourism industry in India and abroad due to worldwide industrial development, increased earnings of individuals, economic growth of tourists producing nations, improved transport and communication means etc. Further, India has multiple plans to promote yoga and meditation, rural tourism, sports tourism, medical tourism, adventure tourism etc. Thus, the future of Indian hospitality and tourism industry seems to be very positive. Therefore, Indian hoteliers should try to develop world class infrastructure and facilities for games to make India the “Destination Next”. All these required more funds to finance current as well as fixed assets.

On the one hand, Indian hotel industry is not performing well and on the other, more working capital as well as fixed assets is required to meet the increased demand of hotel infrastructure in future. Thus, it is necessary for the hoteliers to manage their working capital as well as fixed assets efficiently to enhance their profitability. In this paper, an attempt has been made to know whether hoteliers are succeeded in managing their working capital efficiently or not.

NEED OF WORKING CAPITAL MANAGEMENT IN HOTELS

Working capital management involves the relationship between a firm's short-term assets and its short-term liabilities. The goal of working capital management is to ensure that a firm is able to continue its operations and that it has sufficient ability to satisfy both maturing short-term debt and upcoming operational expenses (Beranek, 1966). The management of working capital involves managing inventories, accounts receivable and payable, and cash. Like any other business, hotels, too have operating cycle which begins with the purchase of supplies and ends with the collection of accounts receivables. Due to this operating cycle, sales do not convert into cash instantaneously. Therefore, sufficient working capital is required to sustain sales activity during the operating cycle period. This capital is required to finance supplies such as stores, spares, crockery, wine and liquor, food materials etc.; to meet out the operating expenses such as salaries, power, fuel etc.; to provide finance during credit sales period and to meet the future contingencies (Hampton, 1989). One of the dimensions in working capital management is to determine the optimal level of current assets and current liabilities. As the higher/lower level of current assets has their respective dangers, so working capital management requires a trade-off between these dangers/costs. More specifically, higher level of current assets strengthens the liquidity position of a firm but weakens the profitability while a lower level of current assets shows better utilization of resources but it may have its own dangers in the form of liquidity crunch (Van Horne,2002). So to reach at a liquidity-profitability trade-off is the ultimate goal of working capital management. Another important dimension of working capital management is related to the financing of current assets. As per prudent practices, a firm has to maintain a desirable balance between long-term and short-term sources of financing current assets. The present paper aims at analysing these dimensions of working capital with special reference to selected 5-star hotels in India.

DATA COLLECTION AND SAMPLE SIZE

The required data has been collected both from primary and secondary sources. The primary data regarding the working capital management practices and policies followed by the selected units have been collected through a questionnaire and supplemented with the information gathered during discussions with the executives of the selected units. However, most of the analysis in this paper is based upon the secondary data obtained from published annual reports of the selected 5-star hotels.

The present study covers 5-star hotel chains belonging to both public as well as private sectors. These are

Name of the Company	Hotel Brand Name
Public Sector:	
(1) India Tourism Development Corporation Limited (ITDCL)	The Ashok
Private Sector:	
1. East India Hotels Limited (EIHL)	The Oberoi
2. Asian Hotels Limited (AHL)	Hyatt Regency
3. ITC Hotels Limited (ITCHL)	Welcome
4. Jay Pee Hotels Limited (JPHL)	Vasant Continental and Siddarth
5. Indian Hotels Company Limited (IHCL)	Taj
6. U.P. Hotels Limited (UPHL)	Clarks
7. Bharat Hotels Limited (BHL)	The Grand
8. Apeejay Surrendra Park Hotels Limited (ASPHL)	The Park
9. A B Hotels Limited (ABHL)	Radisson

Further, the study is confined to a period of 10 years ranging from 2001-02 to 2010-11.

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ANALYSIS OF WORKING CAPITAL

1. Size and Composition Analysis

Keeping in view the nature of hotel business where sales are converted into cash relatively faster, it is reasonable to expect that current assets should constitute a smaller percentage of total assets. Table- I contains the average current assets to total assets ratio in selected hotels. It has been observed that on an average ITDCL, the only public sector unit has been maintaining an exceptionally high CA/TA ratio, which may cause unnecessary blockage of funds and hence poor profitability. This danger seems to be more persistent as the c.v. value is also very low, thereby indicating the instantaneously bad management of current assets in this concern. Before switching over to any conclusion, it is better to look into the composition of this higher level of working capital. Table-II reveals that in ITDCL inventories constitute the largest share as compared to other hotel concerns. This fact has been raising further question marks on the management of current assets in ITDCL as inventories are the least liquid asset. Components wise analysis shows that loans and advances constitute the major portion of current assets in most of the hotels. Further, gross working capital and its components show increasing trend almost in every selected hotel except JPHL which is an indication of the fact that the size and operating activities of the selected hotels are increasing over the period of study. Hotel-wise analysis shows that in EIHL, AHL, ITCHL, UPHL, ITDCL, ASPHL and ABHL, the share of cash, debtors and inventories increased less as compared to increase in share of loans & advances.

TABLE-I

Average CA/TA Ratio (%)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	21.2	14.6	41.4	24.5	44.4	70.7	19.8	39.9	12.3	20	33.8
C.V	30.23	68.28	40.95	45.5	18.91	8.06	28.05	33.74	69.42	16.12	22.87

Source: Computed from the Annual Reports of Hotels – various years

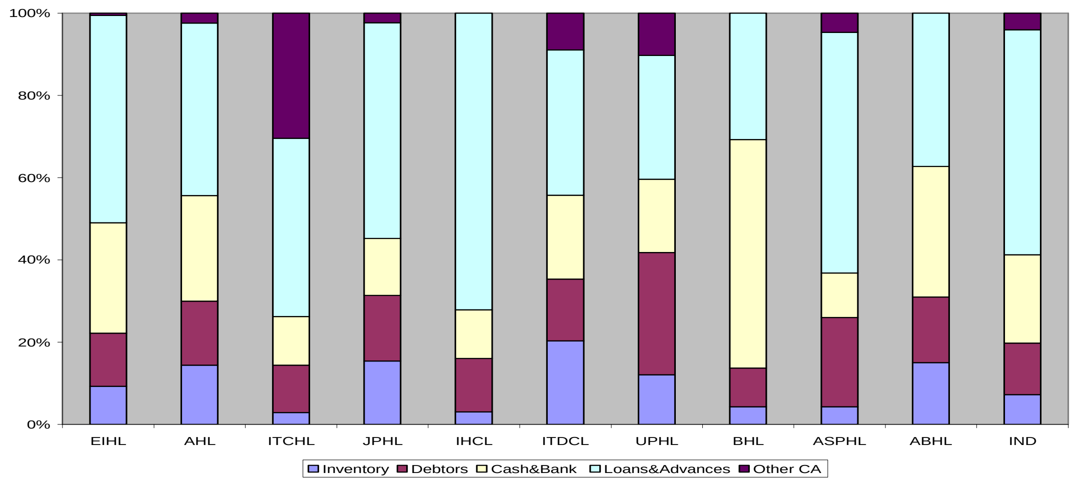
TABLE-II

Average Composition of Working Capital (%)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Inventory	9.26	14.4	2.9	15.4	3.04	20.3	12.1	4.26	4.3	15	7.25
Debtors	12.9	15.6	11.5	16	13	15	29.7	9.44	21.8	16	12.5
Cash&Bank	26.9	25.6	11.8	13.8	11.8	20.5	17.8	55.5	10.9	31.7	21.5
Loans&Advances	50.5	42	43.3	52.5	72.2	35.3	30.1	30.8	58.7	37.3	54.7
Other CA	0.54	2.42	30.5	2.39	0	8.98	10.3	0	4.72	0	4.08
Gross WC	100	100	100	100	100	100	100	100	100	100	100

Source: Computed from the Annual Reports of Hotels – various years

Figure-I Components of Working Capital



2. Financing Working Capital

The way of financing working capital has significant impact on the firm's risk and return. Three basic approaches are available to a financial manager to determine an appropriate financing mix i.e. aggressive approach (A), conservative approach (C) and matching approach (also known as hedging approach). Aggressive approach of financing mix is quite risky leading to high profitability and low liquidity. Under this approach, a firm finances even a part of permanent current assets along with temporary current assets with short-term sources of finance. Conservative approach is less risky leading to low profitability and high liquidity. Under this approach, a firm finances a part of temporary current assets along with permanent assets with long-term financing. The third approach (matching approach) matches the expected life of assets with the maturity of debts raised to finance assets. Thus, fixed assets, and permanent current assets are financed with long-term sources of finance while the temporary current assets are financed from short-term sources of finance.

Table- III
Financing Approach of Working Capital

Name	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
EIHL	A	C	C	C	C	C	C	A	C	C
AHL	A	A	A	A	A	EX.A	EX.A	EX.A	EX.A	EX.A
ITCHL	C	C	C	C	C	A	C	C	C	C
JPHL	C	C	A	EX.A	EX.A	A	A	A	EX.A	EX.A
IHCL	C	C	C	C	C	C	C	C	C	C
ITDCL	A	C	C	C	C	C	C	A	A	A
UPHL	A	C	C	C	C	C	A	A	A	A
BHL	C	C	C	C	C	C	C	C	C	A
ASPHL	C	C	A	A	C	C	C	A	A	C
ABHL	-	-	-	-	EX.A	A	A	C	A	A

Source: Computed from the Annual Reports of Hotels – various years
EX.A – EXTAORDINARY AGGRESSIVE

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The analysis shows that no selected hotel is following matching approach during the period of study. IHCL is following conservative approach throughout the study period whereas AHL has followed aggressive approach in initial years but shifted to extremely aggressive approach from 2006-07 onwards. ITCHL and BHL are also following conservative approach during the period of study except in 2006-07 and 2010-11 respectively when they have followed aggressive approach. Further, JPHL and ABHL are mostly following aggressive or extremely aggressive approach from 2003-04 onwards whereas UPHL and ITDCL have followed conservative approach during the initial years but later on they shifted to aggressive approach.

Thus, it may be concluded that as a whole the selected hotels are trying to shift towards aggressive approach of financing mix in the later years of study which indicates that they want to maintain a balance between liquidity and profitability. However, the selected hotels have not yet succeeded in pursuing the optimal policy of financing the current assets. Keeping in view the nature of hotel industry there should not be any lack of synchronisation between buying inventory, conversion of inventory into finished goods, finished goods into sales and sales into cash. Under such a situation there is hardly any need of keeping a high level of cash and that too from long-term sources to finance. But the selected hotels are unable to keep the operating cycle very short because of low demand of their food and beverage products. The problem has been aggravated by low revenue from room tariff because of low occupancy rate. All these factors are compelling majority of the selected hotels to follow the conservative approach to finance their current assets. It adversely affects the profitability of the hotels. Thus, the hotels will have to overcome the twin problem i.e. low sales of food and beverage products and low occupancy rate with which the Indian hotels are grapping with at present.

3. Ratio Analysis

Ratio analysis is a powerful technique to have insights regarding the level of current assets, financing policy for current assets and utilization of current assets etc. The following liquidity and efficiency ratios have been applied to analyse the prevailing situation in the selected hotels under study:

(1) Liquidity Ratios:

(i) Current Ratio
(ii) Quick Ratio

(2) Efficiency Ratios:

(i) Working Capital Turnover Ratio
(ii) Inventory Turnover Ratio
(iii) Food & Beverage Inventory Turnover Ratio
(iv) Average Collection Period
(v) Cash Turnover Ratio

(1) Liquidity Ratios:

(i) Current Ratio

It may be defined as the ratio of current assets to current liabilities. It measures the ability of the firm to meet its current obligations. Higher the ratio better it is for the liquidity position of a

Table— IV: Current Ratio (Times)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	1.99	1.08	2.42	1.35	3.48	1.84	1.6	1.6	1.37	1.23	2.44
	15.15	35.77	25.64	51.66	13.36	21.82	21.59	21.59	85.42	27.8	7.76
t-Value	4.28*	10.33*	0.01	4.6*	6.85*	4.35*	7.08*	7.08*	-2.69	33.92	

Source: Computed from the Annual Reports of Hotels – various years
* indicates significant t- value at 1% level of significance

concern. However, the ratio of 2:1 is considered quite safe because higher ratio affect the profitability of a concern adversely. But in hotel industry a ratio of 1.5:1 may be considered satisfactory as there is very low level of inventories and high synchronization in comparison to a manufacturing concern.

On the liquidity front, EIHL, ITCHL IHCL and ITDCL are playing quite safe as their current assets are much more than the current liabilities. These hotels, particularly IHCL should bring down the level of current assets. UPHL, BHL, ASPHL and ABHL are maintaining the standard level whereas AHL should improve its liquidity position by increasing the level of current assets or reducing the level of current liabilities.

(ii) Quick Ratio

A more stringent test of liquidity is the quick ratio or acid test ratio. This ratio measures liquidity by considering only quick assets calculated by excluding inventories and prepaid expenses from current assets. Generally, the ratio of 1:1 is considered to be satisfactory to judge short-term financial strength of a firm to pay off its current obligations at time.

Table-V

Quick Ratio (Times)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	1.83	0.94	2.35	1.18	3.37	1.46	1.42	3.54	2.08	1.05	2.25
C.V	18.2	38.89	26.01	61.86	13.93	21.57	23.77	38.12	48.1	26.65	8.57
t-Value	3.8*	10.8*	0.51	4.37*	7.19*	7.46*	7.34*	2.88	-0.5	12.94*	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

From the analysis of the data it has been found that all hotels except AHL, JPHL and ABHL keep the level of liquid assets on higher side. However, ITDCL, UPHL and BHL have reduced the level of liquid assets considerably over the years. Presently, AHL and JPHL are facing the problem of liquidity and IHCL is unnecessarily keeping high level of current and liquid assets continuously. Large amount of loans & advances seems to be the main factor for high volume of liquid assets in IHCL. Thus, almost all the hotels have tried to attain an ideal position to ensure a trade-off between risk, liquidity and profitability.

(2) Efficiency Ratios

(i) Working Capital Turnover Ratio

Working capital of a firm is directly related to sales. The current assets like debtors, inventories, cash etc. generally change with change in sales. This ratio measures the efficiency with which the working capital is being used by selected hotels under study. A higher ratio indicates efficient utilization of working capital and vice-versa. But higher ratio also reflects the lower liquidity position of a firm. However, in hospitality industry with virtually no credit sales and a low level of inventory will generally have an extremely high working capital turnover ratio. This ratio has been calculated by dividing net sales by net working capital.

Table-VI: Working Capital Turnover Ratio (Times)

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	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	3.21	30.76	2.39	12.23	1.39	3.16	14.43	1.32	7.04	105.24	2.02
C.V	32.29	180.45	54.05	114.8	21.21	29.68	102.55	94.26	78.35	227.54	12.19
t-Value	3.45*	1.55	0.86	2.18	6.44*	3.65*	2.52	1.68	2.73	1.29	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

The analysis exhibits that working capital turnover ratio of all the hotels under study recorded a mixed fluctuating trend over the period of study. In AHL and ABHL, the ratio is very high which shows an efficient utilization of working capital in these hotels. The position of this ratio is also good in JPHL, UPHL and ASPHL due to better sales performance as compared to their working capital. However, EIHL, ITCHL, IHCL, ITDCL and BHL are not utilizing their working capital efficiently. It is visible that there is over investment in current assets in IHCL and ITCHL whereas in EIHL, ITDC and BHL, the volume of sales is low as compared to working capital. These claims are well supported by their respective significant t-values of the concerned hotels.

(ii) Inventory Turnover Ratio (ITR)

A firm has to maintain a certain level of inventory to meet the requirements of the business. But the level of inventory should neither be too high nor too low. There are chances of deterioration in quality as well as unnecessary blockage of funds in case of excessive inventory which affects the profitability adversely. Similarly, low inventory may mean loss of business opportunities. Therefore, inventory turnover ratio has been calculated to know how quickly the inventory is being used by the selected hotels under study. A higher turnover ratio means that a firm is able to carry out its business activities efficiently without investing too much money in its inventory and vice-versa. This ratio is calculated by dividing the cost of goods sold by the average inventory.

Table-VII : Inventory Turnover Ratio (Times)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	12.91	18.19	33.96	15.9	24.18	6.32	23.81	15.32	39.6	15.81	20.6
C.V	7.47	26.57	25.71	45.24	16.8	18.01	20.86	25.8	47.72	14.38	58.53
t-Value	24.54*	1.62	4.52*	2.04	2.5	38.17*	1.82	4.16*	2.98	6.58*	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

The results show that ITCHL, IHCL, UPHL and ASPHL are performing better over the period of study. But average ITR of ITDCL, the only public sector unit under study is only 6.32 times well below the industry average of 20.60 times. Thus, the prevailing situation of ITDCL is really very serious and management should take necessary steps to improve the same. Similarly, EIHL has average ITR i.e. 12.91 times well below industry average, so required much attention of management to improve the same significantly. However, the average ITR of other hotels namely AHL, JPHL, BHL and ABHL is not much less than the industry average but required further improvement in the same.

(iii) Food and Beverage Inventory Turnover Ratio (F&BITR)

Food and beverage is the major component of inventory and include fresh food, fruits and vegetables, dry and frozen foods, minerals, wines, beers etc. Thus, the position of selected hotels regarding utilization of inventory is made more clear by way of analysing the food and beverage turnover ratio. This ratio is calculated as follows:

Food and Beverage Inventory Turnover Ratio =Cost of Food and Beverage Used/Average Food and Beverage Inventory

Average Food and Beverage Inventory = Opening and Closing Food and Beverage Inventory/2

Table- VIII: F&B Inventory Turnover Ratio (Times)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	7.79	7.79	9.13	12.52	8.55	2.28	12.68	7.47	34.27	11.58	11.41
C.V	9.11	22.92	24.3	13.83	15.68	29.95	10.21	21.15	144.16	23.44	152.77
t-Value	15.27*	6.07*	3.07	1.95	6.38*	39.99*	2.96	7.45*	1.39	0.2	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

The results indicate that average ratio of ASPHL is 34.27 times as compared to industry average of 11.58 times and has high variability as revealed by its C.V. value i.e. 144.16. Further, the table shows that JPHL, UPHL and ABHL are utilizing their food & beverages inventory more efficiently while EIHL, AHL, ITCHL, IHCL and BHL have shown tremendous improvement over the period of study. But the performance of ITDCL, the only public sector unit is very low continuously as indicated by its average ratio of 2.28 times. The claim is also supported by its most significant t-value. Therefore, management should take some drastic steps to improve its position in this regard.

(iv) Average Collection Period (ACP)

The average collection period measures the quality of debtors by indicating time lag between credit sales and collection thereof. Further, this ratio indicates the effectiveness in formulating credit control policies and their administration. The formula used for calculating the ACP is as follows:

$$\text{A.C.P.} = \frac{\text{Average Debtors}}{\text{Net Sales}} * 365$$

However, it is always advisable to use figures of net credit sales instead of net sales. The reason is that debtors are created only due to credit sales. But the figures of net credit sales were not available for the selected hotels and therefore, net sales have been used in this study. This might have affected the results to some extent but still be beneficial to draw some useful conclusions.

Table-IX: Average Collection Period (Days)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	30	15	32	48	47	43	38	45	36	18	38
C.V	16	25	22	52	11	16	26	17	25	13	6
t-Value	4.91*	18.98*	2.55	1.15	5.18*	2.07	0.04	2.48	0.96	26.05*	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

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The results show that AHL and ABHL have performed better continuously over the period of study with overall average value of ACP i.e. 15 and 18 days respectively as compared to industry average of 38 days. Whereas mean value of ACP is higher in JPHL, IHCL, BHL and ITDCL as compared to industry average. Further, there is continuous increase in ACP in EIHL. However, all the hotels except BHL and EIHL have improved their position in this regard over the years and should continue their efforts to improve further. EIHL and BHL should make more efforts to do speedy collection of debtors.

(v) Cash Turnover Ratio (CTR)

CTR shows that how quickly cash moves through an enterprise's operations. All things being the same, generally the higher CTR indicates better management of cash as well as comparatively low requirement of cash for financing large volume of business operations. CTR has been calculated to assess the velocity of cash in the selected hotels. The formula used to calculate this ratio is as follows:

$$\text{Cash Turnover Ratio} = \frac{\text{Net Sales}}{\text{Average Cash and Bank balance}}$$

Analysis of the data shows that the average CTR of BHL is 1.84 times which is much below the industry average of 6.25 times. This claim is also supported by its significant t-value. This indicates that BHL has failed to use this precious current asset judiciously. The position of EIHL is also not good as compared to industry average. Average CTR of this hotel is 5.93 times.

Table-X : Cash Turnover Ratio (Times)

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
Average	5.93	21.11	12.76	13.45	16.98	8.06	20.65	1.84	23.52	9.76	6.25
C.V	30.89	80.01	46.43	51.73	66.3	49.36	30.43	106.01	36.26	20.6	21.64
t-Value	-0.53	2.64	3.3	3.1	2.86	1.37	6.87*	-6.77*	6.07*	3.9	

Source: Computed from the Annual Reports of Hotels – various years

* indicates significant t- value at 1% level of significance

Thus, BHL and EIHL need to overhaul their approach to make judicious use of cash. However, as the performance of other selected hotels is concerned, all have higher average CTR as compared to industry average. Further, in UPHL, ASPHL and ABHL, this ratio is very much higher than industry ratio. This claim is also supported by their respective significant t-values. Whereas there is high fluctuating trend in this ratio in AHL, ITCHL, JPHL, IHCL, BHL and ITDCL which is also indicated by their respective high C.V. values and even the average CTR of IHCL and ITDCL is declined very sharply in 2003-04. Thus, these hotels need consistency to maintain their better record.

(E) Econometric Analysis of Working Capital

Generally, the quantum of investment in current assets is directly associated with level of operating activities in a firm whereas operating activities with the sales volume. Therefore, to examine the managerial policies/decisions related to investment in current assets, simple regression model has been framed with sales as independent variable and current assets as dependent variable. A regression equation

Y=a + bX has been constructed to find out the regression results. Where
Y= Current Assets
a= The Constant Term
b= Slope Parameter
X= Sales

Table-XI: Regression Results of the Equation Y= a+bX

	EIHL	AHL	ITCHL	JPHL	IHCL	ITDCL	UPHL	BHL	ASPHL	ABHL	IND
a	-108.66	-7.82	63.03	49.36	-301.61	4.37	-5.77	154.37	5.46	0.05	-142.83
b	0.96*	0.33*	0.40	-0.39	1.61*	0.77*	0.59*	-0.38	0.40*	0.34*	0.93*
R	0.86	0.79	0.03	0.18	0.38	0.69	0.43	0.02	0.25	0.75	0.70

Source: Computed from the Annual Reports of Hotels – various years
* indicates significant b- value at 1% level of significance

The independent variable (sales) explains the variation in dependent variable (current assets) to a large extent in EIHL, AHL, ABHL and industry as a whole in comparison to other hotels as indicated by their respective R^2 value. Further, the value of b indicates the quantum of change in current assets due to one unit change in sales. In IHCL, increase in sales resulted into high increase in current assets as indicated by its b value i.e. 1.61 which indicates strong liquidity position but also refers to unnecessary blockage of funds in current assets. Thus, such position impairs the profitability. In EIHL and ITDCL, the investment in current assets also supports the increased sales level to a large extent in comparison to other selected hotels as shown by their respective b values.

Conclusion

On the basis of the analysis made, it can be concluded that current assets constitute about one third of total investment in the selected hotels under study as well as in the hotel industry as a whole. However, ITDCL, the only public sector company under study maintains a very high level of current assets in comparison to other selected hotels. Various factors are held responsible for it. Like other selected units under study, there is low demand of food and beverage products in ITDCL. Whatever demand is there generally it comes from government departments or different ministries. It poses two types of problem for the hotel management. First, it is compelled to keep always a goods stock of inventory to meet the rush orders particularly from the various ministries. Secondly, there are inordinate delays in payment from the concerned offices and to finance the inventories and sundry debtors the management has no alternative except to keep a high level of cash. All these problems add to the cost and losses to the hotels. Further, analysis of different components of current assets makes it clear that on an average, loans & advances constitute a major portion of current assets in all the selected hotels except BHL where cash and bank balances constitute a major portion of current assets.

The analysis of working capital has also revealed that no selected hotel has been following matching approach to finance its current assets. IHCL has adopted strict conservative approach followed by ITCHL and BHL. On the other hand, AHL has extremely aggressive approach followed by JPHL and ABHL. UPHL and ITDCL do not follow any definite policy to finance their current assets.

Current ratio and quick ratio reveal that AHL and JPHL are facing the problem of liquidity and IHCL is unnecessarily keeping high level of current and liquid assets continuously. These factors are well supported by the results of regression analysis. Thus, AHL, JPHL are advised to improve their liquidity position while IHCL should bring down the level of its current assets. Remaining hotels are trying hard to ensure a trade-off between risk and return and consequently to maintain a reasonably good liquidity position.

WTR indicates that AHL, ABHL, JPHL UPHL and ASPHL have a little edge over the other selected hotels in making judicious use of working capital. Further, ITR and F&BITR indicate that ITCHL, IHCL, UPHL and ASPHL are comparatively making good use of inventory while other selected hotels mainly ITDCL and EIHL are found most wanted in this regard. Analysis shows very low F&BITR in ITDCL indicating high inefficiency.

ACP of AHL and ABHL is very low which shows efficient collection policies and better management of debtors in these hotels. But other selected hotels mainly ITDCL, BHL and EIHL should review their collection policies and make efforts to improve it to improve profitability and liquidity. Management of cash is also not efficient in EIHL and BHL as indicated by their respective CTR. In UPHL, ASPHL and ABHL managing cash is not a problem to be highlighted.

To sum up, it may be concluded that five star hotels whether they belong to public sector or private sector are facing problems in managing their current assets well. The burning problems are low inventory turnover, high average collection period, lack of synchronisation and poor approach in financing the working capital. This is particularly true about ITDCL. There is need to increase the volume of sales by creating more demand for food and beverage products and improving occupancy rate of hotel rooms. Steps should also be taken to overcome the problem of lack of synchronisation and to improve the financing pattern of current assets. Efforts should also be made to realise the debtors as quickly as possible.

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