A NEXUS BETWEEN LIQUIDITY/PROFITABILITY TRADE-OFFS FOR WORKING CAPITAL MANAGEMENT IN NIGERIA`S MANUFACTURING SECTOR

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ABSTRACT
This paper is proposes to conceptually explore the meeting point between liquidity and profitability as keys to working capital management. This is deemed very vital especially in the Nigeria manufacturing sector that is in clear need of repositioning .It is therefore vital that a balance has to be achieved between the conflicting objectives of liquidity and profitability. In the efficient and effective management of working capital to ensure the survival of the sector.

Keywords: working capital management, liquidity, profitability, manufacturing sector, and Nigeria.

INTRODUCTION
Decision on either liquidity or profitability is all about planning which is necessary for the efficient working of any organization. The aspect of planning could be viewed from marketing, production, human resource and financial plans. For effective running of any business, there has to be proper flow of funds. This fund is called working capital which is equally defined as the net current assets, or the current assets less the current liabilities (Prasana 2000).

It is therefore clear that, if an organization at any given point in time does not have the enough funds to meet its short-term obligations such as creditors, salaries, and the day-to-day expenses, then it is likely to become technically insolvent. Conversely if the business or firm is so conservative it may have a surplus of working capital, which will adversely affect profits.

Therefore, the trade-off between profitability and liquidity is the key to working capital management, especially in the manufacturing sector. In line with this therefore, we employ the theory of risk and return in trying to explore the options. This theory presupposes that investments with high risks are expected to have a high return while those with low risks potentials will have less returns. Aligning this therefore, to the working capital concept, we can say that if a firm decides to be too liquid, it has tied investment chances and therefore less profit. Conversely if it is decides to engage more of the working capital, it will naturally be less liquid. These decisions are very vital in order to reach an equilibrium between the two for business survival especially in the manufacturing sector.

Malur and Rani (2012) opined that, Business must continuously innovate and transform themselves to stay ahead of competition in the fast growing world. An effective and efficient system of working capital management hast to be evolved to run business and make profits in the long run. In the manufacturing sector especially in Nigeria, costs are ever-increasing, companies therefore have to make efficient use and distribution of finished product to the existing customers.

It is a common fact in most business decision-making situations that certain goals. Where it becomes practically impossible to quantify the exact cost-benefit trade-offs among these goals according to their importance, so that least important ones are only pursued when the most important goals are achieved.

LITERATURE REVIEW

Various studies attempted to proper suitable landing ground for business in dealing with this ever-lingering liquidity/profitability trade-offs.

Coskun et al (2008) In their effort to improving business process, they studied an integrative methods, which involved determining and analyzing the weak points and reducing the weakness degrees. They suggested a four-phase business process improvement framework. Start-up, self analysis, defining improvement strategy for making changes, feedback and continuous improvement strategy for making changes, feedback and continuous improvement. They found that when dealing with decision problems to improve a process, it could be structured to provide input data suitable for multi-criteria decision making techniques. This finding is more related, to finding the solutions through a model.

Jafar and Sur (2006) studied the efficiency of working capital management in the National Thermal/Power Corporation (NIPC), their findings shows that the environmental influence arising from liberalization, globalization and competitiveness has a high influence in the management of working capital. Moreover, Rafuse (1996) in his studies debunked the idea of delaying payment to the creditors as a strategy of improving capital. Instead he proposed that companies should strategize more on stock management based on "lean supply-chain" techniques.

Equally, Cote et al (1999) investigated on the various limitations of traditional measures of working capital management. They therefore proposed based on the past work in finance literature, the introduction of a new ration known as "merchandising ratio". This ratio was used to measure the net effect of firm`s working capital management strategy.

Garaz-Teruel and Martinez-Solano (2007) equally used sample of small and medium-sized Spanish firms to study the effects of working capital management on their profitability, their findings was that, managers stands the chance of creating value by reducing the inventories, and the number of days in which their accounts are outstanding. They equally uncover that the shorter the cash conversion cycle the higher the firm`s profitability.

However, Filbeck and Krueger (2005) in their study found a significant differences in working capital measures between different industries across time, and therefore employ that firm`s should device a means of reducing financing costs, and the funds tied up in current assets.

In addition to that, Chakraborty (2008) studied the relationship between working capital management and profitability of Indian pharmaceutical companies. He concludes a two school of thoughts. The first is that, working capital itself is not a factor of improving profitability, hence there may be a negative relationship between them, the second being that it is the investment in working capital even at minimum level, the sales and output cannot be maintained, and will keep fixed assets inoperative.

Nonetheless, Sigh (2008) discovered that, the size of inventory directly affects working capital management. He concludes that since inventory was the major component of working capital, it needs to be carefully controlled.

Mohammad (2011) studied a sample of 1063 companies listed on Tehran stock exchange to study the relationship between working capital and corporate profitability. He found that there is a negative relationship between numbers of days accounts receivable and profitability.

LIQUIDITY AND PROFITABILTY

Various studied attempted to examine the relationship between working capital management, which embodied liquidity as a component and profitability (Deloof; 2003, Padachi; 2006, Shin and Soenen 1998, and Raheman & Nasr, 2007)

Liquidity in the context of working capital management connotes the tendency of a company, especially the manufacturing company (ies) within the scope of our study, to hold or keep more of cash related, than investing it or using it to the contrary. According to Brealey and Myers (1996). Determining the value of liquidity is one of the 10 unsolved problems in finance.

While the profitability is considered as the front of a business. It reflects the final result of business operations. There are two types of profitability ratios: profit margin ratios and rate of return ratios. Profit margin ratios show the relationship between profit and sales. The two popular profit margin ratios are gross profit margin ratios and net profit margin ratios. Rate of return ratios reflects the relationship between profit and investment. The important rate of return measures are return on total assets, earning power and return on equity (Prasan, 2000).

It is vital to understand that within the context of working capital management, a trade-offs and maintaining a balance between liquidity and profitability is quite necessary for firm`s survival. A manufacturing company must ensure that neither liquidity nor profitability is over-stretched, but rather has to maintain equilibrium. Preferring liquidity to profitability or vice-versa has both advantages and serious repercussions as far as manufacturing firms are concerned.

AN OVERVIEW OF THE NIGERIAN MANUFACTURING SECTOR

Manufacturing remains one of the most powerful engines for economic structure of countries, from simple, slow growing and low-value activities to more productive activities that enjoy higher growth prospects. Jide (2010).

According to Bureau of Public Enterprise (BPE) (2006) Players in the Nigerian Industrial and Manufacturing sector can be classified into four groups, Multinational, National, Regional and Local. However, the Manufacturers Association of Nigeria has categorized its industries into large, medium and small scales in line with the National Council of Industries (NCI) classification Jide (2010).

According to Manufacturers Association of Nigeria (MAN), The Standard Organization of Nigeria (SON), and the Raw Materials Research and Development Council (RMRDC) classification of manufacturing sectors, the following products sectoral groups exist in Nigeria: Food; Beverages and Tobacco; Chemical and Pharmaceuticals; Domestic and Industrial Plastic and Rubber; Basic metal, Iron and Steel products; Pulp; Paper products; printing and publishing; electrical and electronics; Textile; Wearing apparel; Carpet, Leather and Footwear; Wood and Wood products including furniture, Non-metallic mineral products; Motor vehicle and Miscellaneous Assembly. Jide (2010).

Manufacturing in developing countries in general and Nigeria in particular, consist largely of handful of factories producing construction material, clothing, textiles, footwear and processed foods using simple assembly process. With little or no consideration to appropriate working capital strategies especially the balancing between liquidity and profitability.

The United Nations Industrial Development Organization (UNIDO) has reported a decline in the growth of the manufacturing sector in Nigeria and other developing countries. It stressed that manufacturing output in these countries dropped to the lowest level since the beginning of 2011.

Although manufacturing is usually a small sector in African Economics, in terms of share of total output or employment, growth of this sector has long been considered crucial for economic development. This special interest in manufacturing stems from the belief that the sector is a potential engine of modernization, a creator of skilled jobs, and a generator of public spillover effects (Tybout, 2000)

CONCLUSION

The discussion at profitability / liquidity trade-offs has always been in conducive. The motive to strategy and practical existing circumstances are always critical factors that must be considered in maintaining a balance liquidity and profitability.

The bottom line here, must always be maintaining an ideal level of liquidity and profitability in the Nigeria`s manufacturing sector in order to ensure the required growth, stability and survival of sector.

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