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WORKING CAPITAL MANAGEMENT AND COMPANY'S PROFITABILITY: EVIDENCE FROM FOOD AND BEVERAGE COMPANIES LISTED IN INDONESIAN STOCK EXCHANGE

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ABSTRACT

Working capital management is a very important part of corporate finance. If the company's lack of working capital, the company cannot run its operation to the maximum. However, if company had excess working capital, the company will have idle funds. It reduces company's profitability. This problem makes the management must be careful in making decisions related to working capital. Firm may have an optimal level of working capital that maximizes their value.

There are few studies in many countries that show the influence of working capital management to company's profitability. Deloof (2003), Raheman dan Nasr (2007), Ukaegbu (2014) dan Gama (2015), found that working capital management (proxied by average collection period, average payable period, inventory conversion period, and cash conversion cycle) affects to company's profitability. However, Mathuva (2010) dan Vahid et al. (2012) did not find the effect when working capital management was measured using cash conversion cycle. Gill et al. (2010), Napompech (2012), dan Abuzayed (2012) also cannot prove the effect when working capital management was measured using average payable period. Based on the inconsistency of these empirical results, we interested in re-examine the effect of working capital management to company's profitability in Indonesian's food and beverage sector companies that listed at Indonesian Stock Exchange from the period 2009 to 2014.

Data for this study was collected from the food and beverage companies on the Indonesian Stock Exchange for the periods 2009 to 2014. Our study used purposive sampling method. The final sample of this study is 72 firm-years observation. We use the pooled regression type of panel data analysis. Our research had two regression models. In Model 1, we used Cash Conversion Cycle (CCC), which measure comprehensively working capital management, as an independent variable. In Model 2, the three components of working capital management, i.e. Average Collection Period (ACP), Inventory Conversion Period (ICP), Average Payment Period (APP) has been regressed againts the dependent variable. We used ACP, ICP and APP to indicate the company's sales policy, inventory policy and purchasing policy, respectively. To show the effect of working capital management policies on the firm profitability, this study used the return on assets (ROA) as dependent variable.

The results show that the component of working capital management, i. e. Average Collection Period and Inventory Collection Period have negative effect on the company's profitability. Furthermore, we found that Cash Conversion Cycle dan Average Payment Period has not impact on the profitability. Raheman et al. (2010) showed that there are two beliefs which can explain about the relationship between working capital management and profitability. The traditional belief argue that reducing working capital investment would positively effect the profitability of firm by reducing proportion of current asset in total assets (working capital aggressive policy). However, divergent to traditional belief, more investment in working capital might also increase profitability (working capital conservative policy). Our findings provide empirical support for the traditional belief, i.e. working capital aggresive policy.

The results of our study indicate that companies need to accelerate their cash collection and sales to enchance the company's profitability. The management of a company can enchance profitability by reducing the number of days account receivables and inventory turnover. Our findings help the management of a company to choose which working management policy must be implement in the company, in order to enhance the profitability.

***Keywords**: working capital, working capital management, profitability, aggresive policy*

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