Profitability Analysis of Sugar Industry

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Abstract

Every business is established to earn maximum return; therefore there is a need to evaluate profitability analysis of sample sugar factories in Karnataka. To know whether the profits earned by the sample factories is sufficient or not. Also to know whether sample sugar factories fulfil the requirements of shareholders and other stakeholders or not. Profitability analysis with reference to return on investment in sample sugar factories in Karnataka is undertaken. The study for this purpose evaluate the assets turnover ratio and also takes into account takes into account the profit margin of sugar factories.

Introduction

Profitability is ability of a business to obtain return on investment in such a way that which, meets all day to day expenses as well as handsome reserve of it must be kept aside to meet future contingencies and uncertainties. Profitability must be in a position to expand, diversify and modernize the business operations in future. It is profitability of a business which satisfies creditors and shareholders. If the profitability is good then company will be in a position to flourish the business otherwise the company will suffer from many problems.

The surplus available after meeting all direct and indirect expenses and also after meeting operational and non operational expenses and after paying dividend to the preference shareholders and equity shareholders. If the surplus is available it depicts the profitability of a business concerns. There reserve and surplus available makes an organisation financially sound and healthy.

Review of literature

Khudsiya Zeeshan, Syed Azhar, SSrinivasa Murthy1, “Profitability Analysis of Selected Private Equity Funds in India”, the study analyses the solvency and profitability of select private equity funds in India: SequoiaCapital India, ChrysCapital EverstoneCapital Advisors Private, ICICIVentures and West BridgeCapital. Solvency is determined by the debt to equity ratio, interest coverage ratio and proprietary ratio and profitability is determined using ratio such as return on total assets, return on investment and Earning per share. It can be concluded that there are significant differences in terms of the current ratio, debt to equity ratio, proprietary ratio and return on total assets ratio of select private equity funds in India, the test results also indicate that there is no significant difference in terms of return on shareholders funds return on investment and earnings per share. Hence, this ratio analysis is useful management tool to improve the understanding of financial results and Trends over time and can provide key indicators of organisational performance.

S.K. Tanwar, S.S. Chowhan2, “Liquidity Management and Profitability: A Study on Selected Public Sector Companies in India”, the present empirical study is designed to examine and analyse the industry practices in managing liquidity and profitability of the companies with the purpose of examining the performance of management in the area of financial management. The efficiency of
working capital management can be ensured by effective administration of various components of working capital inventory, receivables and cash. This study has attempted to examine efficiency and effectiveness of management in each of these cited areas. Inadequate amount of working capital is an indicator, and not an excuse, but by no means could be the cause of failure of business. The efficient and effective management of liquidity and profitability is, thus, crucially important for success of a business firm. Business firms need to optimise the use of available resources through efficient management of current assets and current liabilities. The present empirical study being designed with analytical approach (instrumental prospective) has dealt with primary and secondary data related to Working Capital Management in the selected public sector companies (such as Bharat Heavy Electricals Limited, Steel Authority of India Limited and Shipping Corporation of India, Shipping Corporation of India, have been collected from respective offices.

**Ambika**³, “A Study on Profitability Analysis of Selected IT Companies in India”, The major objectives of the study are to examine and evaluate the financial performance and financial position of the selected IT companies. To analyse the profitability position of selected IT companies in India. To analyse the liquidity position of selected IT companies in India. To offer valuable suggestions for a better and improve the performance of selected IT companies in India. This study is explorative in nature and based on secondary data. The data for the study consists of various financial statements of selected Companies listed in Bombay Stock Exchange. The selected IT companies have been purposefully selected and used as sample for the study. In total, five companies are finally selected for research namely Tech Mahindra Limited, Infosys Limited, HCL Technologies Limited, Tata Consultancy Services Limited and Wipro Limited. The data has been collected from the official websites of the selected IT companies. The tools used for present study or ratio analysis mean and standard deviation. This study attempts to make to know the financial performance of selected IT companies in India and the overall performance are good.

**Pandit Kumar Kanujiya**⁴, “Analysis of Working Capital and Profitability: An Evident Study of Selected FMCG Companies in India”, in this research paper shows the relationship between Working Capital Management determinants on profitability. Working Capital Management is one of the preconditions for the financial management of any organisation or companies. This research paper the author’s aims maintaining an adequate amount of readily available cash resources in the business for carrying out the daily operations of the company. Profitability is dependent variables whereas determinants of working capital are independent variables such as average collection period, inventory turnover is days, average payment period were used to assess Working Capital Management, and return on total assets. in this study has considered sample of size of five FMCG companies in India over five years period from 2013 to 2017. The analysis done by using OLS Regression show whether there is a significant relationship between these variables.

**Senthil Kumar K., Sengottaiyan A**⁵, “Determining the Profitability of Selected Textile Companies in India”, the objective of this study is to analyse the factors determining the profitability of selected textile companies in India and to suggest measures for effective operations and offer recommendations for the improvement of efficiency in textile industry. In the present study an extensive use of secondary data which are not gathered specially to meet the needs of the problem at hand. for this study, data have been collected for the period of fifteen years from 1997 to 2011. The published annual reports from CMIE PROWESS database and other publications such as stock exchange official directory, Economics Times, Financial Express, RBI Bulletin and other periodical journals have also been used. The sample companies work KSL Industries Limited, Bombay Dyeing Company Limited, Skumars National Wide Limited, Raymonds Limited, Vardhaman Textile Limited, Arvind Limited and National Textile Limited. The profit ratio is measured by sales will give a short term perspective of profitability because sales are annual flows. On the other hand, the return on assets will
gives us long-term prospects of profitability. In this study, the ratio of return on capital employed is used as dependent variable in the specified model.

**Research Gap**

The above review of literatures reviewed, revealed that the study deals with solvency and profitability of select private equity funds of India, the solvency is determined by using debt-equity ratio, interest coverage ratio and proprietary ratio and profitability is determined using return on total assets, return on investment and Earning per share.

The study deals with liquidity management and profitability. The efficiency of working capital management can be ensured by effective administration of various components of working capital, inventory, receivables and cash. The efficient and effective management of liquidity and profitability deals with management of current assets and current liabilities.

The study deals with profitability analysis of selected IT companies in India, this study is explorative in nature and based on secondary data. The data for the study consists of various financial statements of selected Companies listed in Bombay Stock Exchange.

The study deals with analysis of working capital and profitability. The study shows the relationship between Working Capital Management and determinants on profitability. The profitability is a dependent variable, whereas working capital is an independent variable. The analysis done by using OLS regression show whether there is a significant relationship between these variables.

The last study deals with determining the profitability of selected textile companies in India. The objectives of the study are to analyse the factors determining the profitability of the selected textile companies and to suggest measures for effective operations and offer recommendations for the improvement.

It can be said that various works have been undertaken on profitability analysis on equity funds, public sector companies, IT companies, FMCG companies and textile companies, but profitability analysis of sugar industry in Karnataka is scanty. Therefore there is a need to study the profitability analysis of select sample sugar factories in Karnataka. The study deals with return on investment in sample sugar factories in Karnataka.

**Statement of the Problem**

Profitability analysis with reference to return on investment in sample sugar factories in Karnataka is undertaken. The study for this purpose evaluate the assets turnover ratio and also takes into account takes into account the profit margin of sugar factories.

**Objectives of the Study**

- To evaluate the profitability with reference to return on capital in sample sugar factories in Karnataka.
- To offer suggestions.

**Need for the Study**

Every business is established to earn maximum return; therefore there is a need to evaluate profitability analysis of sample sugar factories in Karnataka. To know whether the profits earned by the sample factories is sufficient or not. Also to know whether sample sugar factories fulfil the requirements of shareholders and other stakeholders or not.
Scope of the Study

The study covers only select sugar factories in Karnataka and excludes all other public and co-operative sugar factories from the study. At the same time the period is confined to 10 years starting from 2005-2006 to 2014-2015, and the performance of selected factories before and after study period excluded.

Research Design

The study is nature of desk research.

Sources of Data: The data required for the study collected from secondary source. The secondary data obtained from the Annual reports of the selected factories; magazines, Government reports, newspapers, internet surfing etc.

Sample Design: As on October 2011, the population for the study comprises of 38 private sugar factories in Karnataka. With the use simple random sampling technique the researcher selected10 Sugar factories in the Karnataka State. However due to non-cooperation of two factories (GEM and Jamkhandi Sugars Limited) in providing data they have been out of the study. This leaves eight factories as sample and represents the sugar industry. The sample factories are given below:

1. Parrys Sugars Limited (Parrys)
2. ShriPrabhulingeshwara Sugars and Chemicals Limited (Prabhulingeshwara)
3. Shree Renuka Sugar Limited (Renuka)
4. The Ugar Sugars Works Limited (Ugars)
5. Athani Farmers Sugar Factory Limited (Athani)
6. DavangereSugar Limited (Davangere)
7. Sri Chamundeshwari Sugar Limited (Chamundeshwari)
8. Bannari Amman Sugars Limited (Bannari)

Here on words the sample factories are called in short names.

Tools of Analysis

The data collected analysed with the help of ratio analysis, trend analysis and statistical techniques wherever necessary to draw meaningful inferences.

Limitations of the Study

The figures taken from the annual reports have been rounded off to two decimals of rupees in Lakhs. The data available in financial statements have been translated into pre-designed the structure format so that a meaningful interpretation could be made through inter-firm and intra-firm comparison. The format in which data have been classified is selected after carefull consideration of the operations of the sugar factories. Nevertheless, the limitations do in No way act as a deterrent in drawing effective and meaningful inferences from this study.

Analysis of Profitability with Reference to Capital Invested

Profit indicates the ‘commercial ability' of a concern, but it does not indicate the level of efficiency of an undertaking. The efficiency of an undertaking cannot be judged by considering the volume of profits, without taking into account the size of investment. However, the degree of profitability helps in establishing a quantitative relationship between profit and volume of sales or the level of investment. To measure the efficiency of a concern, profit should be studied in relation to the amount of capital invested.
The most popularly used measure of profitability is to relate the profit output with the capital input and thus, compute the rate of return on capital invested. The return on investment is calculated as mentioned below:

\[
\text{Return on Capital Invested (ROI)} = \frac{\text{Profit Before Interest and Taxes}}{\text{Total Assets} - \text{Intangibles}} \times 100
\]

(or)

\[
\text{Return on Capital Invested (ROI)} = \frac{\text{PBIT}}{\text{Sales}} \times \frac{\text{Sales}}{\text{Total Assets} - \text{Intangibles}}
\]

(or)

\[
\text{Return on Capital Invested (ROI)} = \text{Profit Margin} \times \text{Assets Turnover}
\]

ROI is the result of the multiplication of the above two variables - profit margin and assets turnover, which by themselves are the products of a series of variables denoting various phases of business operations carried on during a given accounting period. Rapidity of the turnover of capital invested and profit margin are the two factors on which profitability of capital invested depends.

Return On capital invested (ROI) denotes how well the management has used the funds supplied by the creditors and owners. Apart from this, it shows earning power of the operating assets. The higher the ROI ratio, the more efficient the enterprise is in using the funds entrusted to it. This ratio provides an indication of the economic productivity of the capital. To put it in nutshell, ROI is the key indicator of overall profitability of an enterprise.

The Du-Pont chart used by the (see Figure 1) Du Pont Company of the U.S. pioneered system of financial analysis, which has received widespread recognition and acceptance. This analysis of profitability with reference to capital employed has been applied for (ROI) in the present study.

![Figure 1 Du Pont Chart](image)

The left-hand side of the Du Pont chart shows the determinants of net profit margin ratio and right hand side throws light on the total assets turnover. A comparison of the ratio of ROI of a firm with the individuals and the aggregate of similar firms over a period of time would provide sufficient insight into how efficiently the funds of owners and creditors are used. The overall profitability will improve if assets turnover or profit margin or both increase.

**ROI in Sample Sugar Factories**

Table-1 presents ROI and its components of combined position as well as individual factories. The ROI of sugar industry in Karnataka state had slid down from 12 Per cent in 2006 to one Per cent in the last year of the study period, on an average the
(ROI) being seven Per cent. In this context, it may be recalled that the standard norm is 10 - 12 Per cent, suggested by Winston and bring them. Hence, the sugar industry profit performance was below the standard level. This clearly indicates that the sugar factories have enjoyed better returns on their resources during the years from 2006 to 2013, but afterwards the profit performance was totally uncomfortable.

Year-wise Analysis of ROI performance of sugar industry reveals a marked inconsistency. This happened due to declined assets turnover coupled with deteriorated profit margin. The factors that attributed to decrease the Asset turnover rate are falling sales, which was due to market uncertainties, production interruptions due to frequent power cuts, raw materials shortage, use of out-dated technology and improper monitoring and control operation cost which led to decline in profit margins ratio.

An Analysis of individual factories reveals that only Bannari have registered on an average ROI of 10 per cent. This factory had exceeded not only the industry but also reached the standard norm of 10 – 12 per cent. The ROI of Parrys, Prabhuligeshwara, Renuka, Ugar, Davangere and Chamundeshwari was 3.33 per cent, eight per cent, six per cent, five per cent, 6.1 per cent eight per cent and 6.3 per cent respectively, which is below minimum standard norm of ROI. There exist disparities in the ROI of sample sugar factories. Analysis of the ROI performance of individual factories is undertaken to find out the reasons for such disparities in profit performance.

**Parrys**

Inspite of variations in ROI, the Parry factory had occupied lowest position with 3.33 per cent on an average. The ROI of the factory varied between the minimum of negative four per cent in 2010-11 and maximum of 14 per cent in 2006, thereby reflecting poor profit performance. The reasons for inconsistency of ROI were continued demand recession supply and demand imbalances. The assets turnover and profit margin, on an average, were registered 0.44 times and 6.2 per cent respectively. These ratios have declined than the combined picture. However, the profitability performance was dissatisfied due to high operating expenses and lack of capacity utilization (Table 7.1).
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### Bannari

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**Note:**
- i) Return on Capital Invested and Profit Margin is Expressed as Percentage.
- ii) Assets Turnover is Expressed as Number of Times.

**Source:**
- i) Appendix - I (A) to I(I); and
- ii) Appendix - III (A) to III(I).
Prabhulingeshwara

The factory had recorded on an average ROI of eight per cent, which is nearer to the minimum standard level. The assets turnover and profit margin have oscillated from a minimum of 0.60 times in 2006 to the maximum of One times in 2011 and from five per cent in 2013 to 23.74 per cent in 2008 respectively. Consequently, ROI had also varied from four Per cent to 14 per cent over the years. The assets turnover had varied throughout the study period under reference. The profit margin had declined continuously accepting 2008 over the years under study. The factors responsible for this decline in profit margin are: adverse market conditions in the sugar board sector and an increase in interest rate and financial charges. Further, the factors attributed to the continuous decline in ROI over the study period are: increase in cost of goods sold, depreciation, administrative and selling expenses and other high financial costs. The factory’s ROI performance was very poor at the end of last two years of the study. This was due to unfavourable market conditions, delayed stabilization of new facilities, excess capacity in the domestic and international markets, sluggish demand and growth because of fierce price competition, high interest and depreciation charges.

Renuka

The Renuka’s overall profit performance (ROI) recorded, on an average, six per cent, which is far away from minimum standard norm. The ROI ranged from the minimum negatively five per cent in 2015 to the maximum of 13 per cent in 2006. The two components of ROI-assets turnover and profit margins-were marked with oscillations. The variation in the former ranged between 0.62 times in 2009 to 1.12 Times in 2006 and later from negatively five per cent in 2014 to 13.70 per cent in 2009. The factory had registered 13 per cent in 2006. The factory’s ROI had suddenly started to decline from 13 per cent in 2006 and reached as low as negatively five Per cent in 2014. The reasons responsible for the lowest ROI are: decline in assets turnover due to weak economic conditions and recessionary trend prevailing in the most of the industries and steep competition prevailing in the market. However, the factory’s management was trying hard to reach standard norm of ROI.

Ugar

Ugar recorded five per cent of ROI on an average, which is a faraway from the minimum standard level. The assets turnover and profit margin have oscillated from a minimum of negative 0.29 times in 2010 to the maximum of 1.1 times in 2013 and from negatively 0.98 per cent in 2010 to maximum of 11.80 per cent in 2009 respectively. Consequently ROI had also varied from negatively one per cent to nine per cent over the years. The assets turnover had declined continuously over the years under study. The profit margin had been decreased continuously over the year under study except in 2009. The factors responsible for this decline in profit margin are: adverse market conditions and an increase in interest rate and Finance charges. Further, the factors attributed to the continuous decline in ROI over the study period are: increase in cost of goods sold, depreciation, administrative and selling expenses and other financial costs. The factory’s ROI performance was very poor at the end of the last two years of the study. This was due to unfavourable market conditions, delayed stabilization of new facilities, excess capacity in domestic and international markets, sluggish demand and growth because of fierce price competition, high interest and depreciation charges.

Athani

Athani’s overall profit performance (ROI) recorded, on an average, six per cent, which is below the minimum standard norm. ROI ranged from the minimum of three Per cent in 2015 to the maximum of 10 per cent in 2009. The two components of ROI-assets turnover and profit margin- were marked with oscillations. The variations in the former ranged between 0.31 times in 2015 and 0.89 times in 2012 and later from 10 Per cent in 2015 to 19.15 per cent in 2006. The factory had registered 10 per cent ROI in 2009. The factors responsible for this are: high sales turnover with better product mix coupled with improved market demand and low operating costs. The factory’s ROI had suddenly started to decline from 10 per cent in 2010 and reached as low as three Per cent by the end of the study period. The reasons responsible for the lowest ROI are: decline in assets turnover due to weak economic conditions and
recessionary trend prevailing in the most of the industries and steep competition prevailing in market. However, the factory’s management was trying hard to reach standard norm of ROI.

Davangere

The factory had recorded on an average ROI of eight per cent which is nearer to minimum standard level. The assets turnover and profit margin have oscillated from a minimum of 0.55 times in 2015 to the maximum of 1.17 times in 2011 and from negatively two per cent in 2015 to the maximum of 17.83 per cent in 2007 respectively. Consequently, ROI had also varied from negatively one per cent to 11 per cent over the years. The assets turnover had been variated continuously over the years under the study. The profit margin had been constant in initial five years and then declined to negatively one per cent. The factors responsible for this decline in profit margin are: adverse market conditions, and increase in interest rates and financial charges. Further, the factors attributed to the continuous decline in ROI over the study period are: increase in cost of goods sold, depreciation, administrative and selling expenses and other high financial costs. The factory’s ROI performance was very poor at the end of last one year of the study. This was due to unfavourable market conditions, delayed stabilization of new facilities, excess capacity in the domestic and international markets, sluggish demand and growth because of fierce price competition, high interest and depreciation charges.

Chamundeshwari

Chamundeshwari recorded 6.3 per cent of ROI on an average, which is far away from the minimum standard level. The assets turnover and profit margin have been oscillated from a minimum of 0.31 times in 2008 to the maximum 0.76 times in 2011 and from three per cent in 2015 to the maximum of 22.5 per cent in 2006 respectively. Consequently, ROI had also varied from two per cent to 13 per cent over the years in the study. The assets turnover had been declined continuously except in 2010 over the study under reference. The profit margin had been variated over the years under the study. The factors responsible to this decline in the profit margin are: adverse market conditions and increase interest rate and financial charges. Further, the factors attributed to the continuous decline in ROI over the study period are: increase cost of goods sold, depreciation, administrative and selling expenses and other high financial cost. ROI performance was very poor at the end of the last two years of the study. This was due to unfavourable market conditions, delayed stabilization of new facilities, sluggish demand and growth because of fierce price competition, high interest and depreciation charges.

Bannari

Bannari had occupied first position with regard to ROI with average ratio of 10 per cent on an average, which has reached the minimum standard level. ROI ranged between four per cent in 2015 and 17 per cent in 2010 thereby reflecting irregular behaviour. ROI in the initial year was higher than the standard norm because the factory enjoyed high assets turnover and high profit margin. From 2007 onwards, ROI started to decline and reached four per cent in 2008 due to decline in the assets turnover and profit margin. Again, it had shown it had shown a sudden rise in the year 2009 with 14 per cent and it continued till 2010. During this period, the factory’s management was able to manage the operating cost at lowest level of the all the years of the study period. Thereafter, it had declined from 17 per cent in 2010 and reached to four per cent by the end of the study period. It is disconcerting to note that there was no relation between assets turnover and profit margin. Assets turnover and profit margin declined due to higher power cuts, slackness in the sugar market, continuous recession and severe competition. To sum up, the average ratio of ROI of Bannari was reached to minimum standard norm. It implies that the overall profit performance of this factory was comfortable. The reasons are: favourable demand for finished sugar, realization of better sale prices, effective utilisation of total assets and good profit margin. Further, all the sample factories registered the lowest ROI in the last two years of the study period, which was less than the minimum standard norm. The factors responsible for this situation are: sluggish market demand, price competition, recessionary trend prevailing in the most of the industries and high interest rate and financial charges. Sugar industry as whole and individual factories have reported wide
fluctuations year-wise in the profit performance. Only one factory is able to generate adequate profits since they acted positively to changing face. But majority of the sample factories selected for the study did fail, as the management of these factories were not vigilant.

Finding of the study

- The overall profitability position of sugar industry in Karnataka state had shown declining return on capital invested during the study period. It indicates that the overall profit performance of the sample sugar factories was uncomfortable and it is behind the hope and expectations of all stakeholders. The overall profitability position of sugar industry shows on an average was seven per cent of ROI which is lower than standard than norms of 10-12 per cent during the study the period under reference. The ROI of sample sugar industry was thin because of decline in capital turnover rate.
- Performance of sugar industry with reference to ROI exhibits intense disparities. The overall profitability of sample sugar factories was inconsistent. An analysis of individual sugar factory on an average that the ROI was satisfactory in Bannari and Davangere. The ROI of all other sample sugar factories was thin. Especially Parrys had very thin ROI on an average of 3.33 per cent among all sample sugar factories under the study period.

Suggestions for the Study

- The practice of diversion of working funds for financing long-term assets shall altogether be stopped. This will help in improving the working capital condition of the factories. In fact, the generation of internal funds through fair profit performance and their diversion for current assets financing ensures strong liquidity of the sample factories.
- The sample factories are desperate need of financial support from commercial banks to augment their working capital funds. Commercial banks ought to provide working capital funds liberally at concessional rates of interest at least for a temporary period to tide over the present working capital crisis. Return on investment in the sugar industry has shown a declining trend. Shooting prices of inputs have put a severe strain on the sugar industry resulting in the inflated operating ratio. Therefore, the need of the hour is the effective control of operating costs. Adoption of profit planning and control techniques such as marginal costing, cost-volume-profit analysis, standard costing, activity based costing And flexible budgetary control system may enable the factories to push down the operating costs and boost up the profits.
- The quantum of sales should be improved progressively in order to maintain better capital turnover ratio and to enjoy higher returns on investment. To this end, qualitative sugar, which has high demand in the market, has to be produced.
- Cost of production of sugar per tonne of sugar manufactured has increased abnormally due to high operating costs and the phenomenal increase in the cost of inputs. Production of sugar at low-cost may be possible through the higher utilisation of capacity.
- Increase the price of sugar is one way to increase profits. Raising the prices of sugar is in the hands of Government. So, the Government should play a positive and constructive role while fixing sugar prices taking into account the realities. Otherwise, the sugar industry should be given freedom to fix selling prices of different varieties of sugar by prescribing a broader criterion for arriving at realistic selling prices.
- The main constituents in total cost of goods sold or administrative and selling expenses in sample factories. The amount spent on these, per tonne of sugar sold, has been very high. Excess expenditure in this area is also one of the reasons for low profit performance. So, factories have to reduce administrative and selling expenses.
- Shareholders of some of the sample factories are less satisfied about the performance of the factories, because of the absence of regular dividend. This trend is not conducive for further expansion of the industry. Therefore, the management of these
factories should put in sincere and committed efforts to improve the profitability of the factories to ensure fair return on shareholders.

Conclusion

Overall profitability performance of sugar industry in Karnataka state had shown declining trend in return on capital employed invested during the study period. However, Bannari have enjoyed better return up to 2013 and thereafter the profitability had tended to decline and other sample factories return on capital employed is below the minimum standard norms. It was due to weak economic condition and recessionary trend prevailing in the industries and steep competition prevailing in the sugar market which led to low sales price realisation. The uncomfortable ROI may lead to dissatisfaction of the stakeholders of the industry. As regards the individual factories, the ROI was comfortable in Bannari and uncomfortable in the other seven sample factories under observation. The industry’s sales trends have depicted an overall rise with oscillation over the study period. But with regard to the individual factories, the sales trend registered a normal growth. There was no relation between sales and gross profit, since the increased sales did not lead to increase in gross profit in the industry and in all the selected factories.

Reference


