

# Receivables Management in Public Sector Textile Industry of Bangladesh

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## INTRODUCTION

The word *credit* is derived from the Latin word *Credare* which means to believe or to trust when a seller of goods or services extends credit facility to a customer, mutual trust is implicit in the transaction. If a business firm sells its products or services and does not receive payment then and there, the firm is said to have extended trade credit to customers. Trade credit, thus, creates receivables or book debts, which the firm is expected to collect in the future.

Receivables generally occupy an important position in the structure of gross working capital. The quantum of investment in receivable is the inter-related function of sales, credit collection policies and cash discount. Since this function involves the final stage in working capital cycle (conversion into cash of receivable); it is of prime importance. More specifically, the productivity or turnover of gross working capital largely depends on the productivity or turnover of receivables. Even if purchasing, production and sales are efficiently conducted, careless credit and collection policies will result not only in losses owing to bad debt, but also in the freezing of a large amount of funds into slow moving and doubtful receivable. Consequently locks up the firm's funds, necessitating borrowings from bank and other sources. It has, therefore, a cost and require careful analysis and proper management. Therefore, the basic goal of credit management is to manage its credit in such a way that sales are expanded to an extent to which risk remains within acceptable limit. And, despite its importance we find that it is the most neglected area in public sector textile industry of Bangladesh. So far, the present study is an attempt to fill-up this gap.

The objective of the present study is to make an attempt to analyse and evaluate the receivables management in public sector textile industry of Bangladesh. Thus the study covers all the 40 textile units working under the administrative control of Bangladesh Textile Mills Corporation

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(BTMC). The study is related to a period of ten years starting from 1982/83. The study is mainly based on published annual reports and accounts, and other related publications of the Ministry of Textile. In addition, the researcher visited five operational units of BTMC and collected views from the executives through interview schedule to supplement the factual position regarding the management of receivables in BTMC.

To penetrate into the reality of the problems, the researcher divided receivables into two groups viz. *accounts receivables* and *other receivables*, the former refers to amount owed by customers and the latter to amount owed by employee and other, i.e. advances and prepayments.

## ANALYSIS AND OUTCOME

### Size of Receivables and Its Relative Share in Total Current Asset

The analysis of the size and growth in receivables over a period of time in addition to its share in total current assets can provide a meaningful picture of the current funds invested in the component of current assets. An enterprise is said to be successful if it can operate with the lowest value of receivables to current assets without affecting its sales volume. Thus, the percentage of receivables to current assets can act as a measure of the efficiency of receivables management.

Appendex Table 1 depicts that in absolute amount receivables increased to TK (Bangladesh Currency) 104 crore by the end of 1991/92 as against TK 61 crore in 1982/83. In relative terms receivables ranged between 28.6 percent in 1984/85 to 42.8 percent in 1986/87 of the total current assets with an average of 25.4 percent during the period of study while, there had been wide fluctuation both in absolute terms and in relative terms. Another revealing feature is that the receivable ratio had a tendency to decline over the period. It declined from 40.9 percent in 1982/83 to 29.5 percent in 1991/92, judged also interms of absolute amount, the rate of increase was lower, 1.7 times, in the case of receivables than that of total current assets, 2.4 times, over the 10 year period.

Appendex Table 4 shows that the fluctuation was higher in current assets, C.V. 22 percent, than in receivables, C.V. 16 percent. The table witnesses that the correlation of the above two variables was positive, .706, during that period.

't'-test has been applied to examine whether the correlation is significant or insignificant. Our null hypothesis here is that the correlation coefficient of the above two variables is zero. It is observed that the calculated value of 't' is 2.818, while the critical value of 't' at 5 percent level of significance with 8 degrees of freedom is 2.306. Thus, the correlation was significant as our null hypothesis is rejected.

The inference is that there seems to be good amount of money locked-up in receivables as it was more than one-third of the total current assets on an average. As the Corporation suffered losses throughout the period and felt acute shortage of funds either for operations or for expansion activities, the over investment in receivables to such an extent was not desirable. It demonstrates a weak credit management and lax collection policies.

### Structure of Receivables

In order to be able to ascertain where excess funds were locked-up, it is worthwhile to analyse the composition or receivables in BTMC during the period of study. In BTMC, receivables consist of *accounts receivable*, A/R, and *other receivables*, O/R. O/R is made of advances, deposits and prepayments, etc., It has been the policy of the BTMC to keep minimum investment of funds in its O/R. However, actual position as shown in Appendix Table 2 was contrary to its avowed policy. It is evident from the Appendix Table 2 that O/R constituted 49-89 percent of the total receivables (T/R) during 1982/92. The share of O/R was high, more than four-fifth, particularly in the second half of the study period. In other words, only one-fourth or less than one-fourth of the T/R arose out of credit sales during the same period, 1987-92.

Appendix Table 4 portrays that the fluctuation was too high in A/R, C.V. 57 percent, then that of O/R, C.V. 30 percent. The table also witnesses that the correlation between total receivables and other receivables was positive .651, and the same is significant at 5 percent level of significance with 8 degrees of freedom. Another notable feature was that the correlation between T/R and A/R was positive, .434, but the same is insignificant at 5 percent level of significance with 8 degrees of freedom.

Thus, it is clear from the above that O/R dominated the composition of T/R in almost all the years. Furthermore, in the second half of the study period A/R had noticed a decreasing trend and the

opposite was true in the case of O/R. It is obvious that BTMC should take steps to bring down the investment in O/R so it can invest more to promote both sales and profit.

### Turnover and Average Conversion Period of *Total Receivables*

The turnover of receivables provides information on the liquidity of the receivables. It is calculated by dividing sales with average receivables. The receivable turnover gives a general measure of the productivity of receivables investment. The higher the turnover rate, the more effective and more rewarding the use of receivables. Management of receivables also depends upon the collection policy of receivable. It is to be noted that the measure of receivables conversion period is similar to the measurement of receivables turnover. Both measures yield a similar conclusion. The only difference is the whenever there is a decline in receivables turnover, there is an increase in average collection period and vice-versa.

Appendex Table 3 presents turnover and average collection period of the total receivables in BTMC during 1982-92. The turnover of total receivables ranged between 3 and 5 during the 10 year period. This reveals a liberal credit policy being followed by the Corporation. However, there was a moderate improvement, tightening-up, in the credit policy in the second half of the study period.

The average conversion period also reveals the same story. This ranged between 73 and 121 days during the period of study. Further, average conversion period which ranged between 80 and 121 days in the first five years started declining so much so that by the year 1990/91 it came down to 73 days. These facts also lead us to conclude that although the Corporation followed a liberal credit policy during the entire period of study, but over the years there had been some tightening-up towards the closing years.

The above conclusion is based on the total receivables. But in order to examine the credit policy, it would be more appropriate to analyse the *accounts receivable*, A/R, instead of *total receivables*, T/R. For, it is the A/R which is related to credit sales and not the *total receivables*. Thus, the following analysis relates to A/R which is part of *total receivables*.

### Turnover and Average Collection Period of *Accounts Receivable*

It indicates the speed with which *account receivable* are converted into cash or cash equivalent. The higher the *accounts receivable* turnover, the more favourable it is. The high turnover usually increases profitability. A high turnover of inventory should be supported by a higher turnover of A/R, otherwise the firm may experience heavy loss owing to increased volume of bad and doubtful debts. But high turnover may be due to restricted credit policy, which will certainly affect both sales and profit adversely.

Another important A/R ratio is the average collection period. It is a significant measure of collection activity and the quality of accounts receivable. It indicates how many days needed to convert A/R into cash. It is the concluding stage of cash cycle in an enterprise. A higher collection period compels the enterprise to invest a huge amount in A/R and also increases the possibility of bad debt losses. Therefore, the shorter in the average collection period, the better the credit management and the liquidity of accounts receivable. The increase in average collection period over time would indicate liberal credit policy adopted by the enterprise. With this back ground, the types of credit policy being followed by BTMC are analysed below.

Appendix Table 3 shows that A/R turnover ranged between 6 and 39, as against 3 and 5 in the case of total receivables, during the period of study. The ratio which declined from 13 in 1982/83 to 9.9 in 1987/88 jumped up to 21.7 in 1988/89. There it had further rising trend. The sudden increase from 1988/89 onwards was the result of a steep decline in A/R. This shows that credit sales policy which used to be liberal upto 87/88, was tightened up considerably thereafter.

Average collection period which used to be nearly one month in the beginning years, increased to nearly two months by the mid eighties but then declined to less than half month by the closing years of the study. This also demonstrates the tight credit sales policy being progressively followed by the Corporation. In fact, 9 days or 12 days collection period shows very low investment in A/R. A most surprising point is to note that the correlation between sales and accounts receivable was negative, -0.681, and the same was significant at 5 percent level of significance with 8 degrees of freedom.

In short, foregoing analysis of the total receivables and A/R show that BTMC used to follow a more liberal credit policy in the first half of the study period, but in the second half the same was tightened up. In fact, A/R constitutes a very low proportion in the total receivables, nearly 11 percent towards the closing years, as also total sales, 3 to 4 percent. This is quite obvious that the BTMC's credit sales are limited only to government departments/ organisations.

### **Bad Debt Losses**

Bad debt is the natural outcome of credit sales and credit policy. It arises when a firm is unable to collect its trade receivables. It can be expected to increase with liberal credit policy and decrease with stiff or restrictive credit policy. Change in credit policy can also bring change in the volume of sales. The extenuation of trade credit has a major impact on sales, costs and profitability. Other things being equal, a relatively liberal policy and, therefore, higher investment in receivables will produce larger sales. However, cost will be higher with liberal policies than with more stringent measures. Therefore, *accounts receivable* management should aim a trade-off between profit benefit and risk cost.

The success of the management in keeping down its bad debt losses can be judged by relating them to credit sales. This ratio is generally recognized as a measure of net consequence of credit decisions.

Surprising and noteworthy feature of credit management in BTMC is that there was no bad debt during the whole period of study. As pointed out earlier, it is the policy of the BTMC not to sell goods on credit basis except to the government organisations and other public sector organisations. This was the reason why there was no bad debt at all. All credit sales are collected though in some cases the collection is delayed. Zero bad debt also reveals the tight policy being followed by BTMC in regard to its *accounts receivable*.

### **CONCLUSION**

On the basis of the above analysis and interpretation of empirical data and the researcher's own experience from the field survey, the following conclusion can be drawn:

Receivables management has been found to be in a poor shape in BTMC. The total receivables constituted more than one-third of the total current assets. Further, of the total receivables, *other receivables* like loans,

deposits, and prepayments etc. constituted as high as 49-89 percent with an increasing trend. while *accounts receivable* accounted for only 11-51 percent. The share of *accounts receivable* was considerably low, around 11 percent, particularly towards the closing years of the study.

The turnover of *accounts receivable* was very high, while the turnover of *total receivables* was low and unsatisfactory. The opposite of this was true in the case of average collection period. This situation was due to heavy increase in advances and prepayments and sharp decrease in *accounts receivable* over the period. As regards *accounts receivable*, BTMC had followed a conservative and restricted credit sales policy, while, BTMC had lax control in the field of advances and prepayments.

BTMC management should try to impose strict control over other receivables to keep it within normal limits so that it can invest more for extending trade credit. Furthermore, BTMC's credit sales are limited only to the government departments/organisations. But under the changing business environment which is characterized by globalisation and increasing competition, BTMC must reorient its credit sales policy. In other words, the Corporation should start extending credit sales facilities to private parties also on favorable terms. This will help to boost up sales and profits of the Corporation.

The productivity or turnover of current assets largely depends on the productivity or turnover of receivables as they occupy a significant position in the structure of current assets. Against this background, the present has study strived to evaluate the receivables management in Bangladesh Textile Mills Corporation (BTMC) for a period of 10 years (1982-92). The study has demonstrated very low productivity and poor management of the same. Moreover, it has depicted that other receivables constituted more than four-fifth of the total receivables particularly in the second half of the study period. In fact, *accounts receivable* constituted a very low proportion in the total receivables, nearly 11 percent towards the closing years, as also total sales, 3-4 percent. More surprising is that there was significant negative correlation between A/R and sales. Lack of investment in trade-credit in today's fast-moving, technologically advanced and competitive market place may bring certain death of the Corporation due to over investment in unsold finished goods. It is obvious that BTMC should take immediate steps to bring down the investment in O/R so that it can invest more in A/R to promote both sales and profit.

## APPENDIX

**Table 1**  
**Size and Growth in Current Asset (CA), and Total Receivables (T/R),**  
**and T/R as Percentage of Current Assets in BTMC During 1982-92**

Year	Current Asset (Crore TK)	Change over base year (percent)	Total Receivables (Crore TK)	Change over base year (percent)	Total Rec. as percent of CA
1982/83	149.7	100.0	61.3	100.0	40.9
1983/84	207.9	138.9	69.2	112.9	33.9
1984/85	265.5	177.4	76.0	124.0	28.6
1985/86	237.0	158.3	85.2	139.0	30.9
1986/87	238.9	159.6	102.3	166.9	42.8
1987/88	215.8	144.2	19.5	149.3	42.4
1988/89	226.2	151.0	85.9	140.1	38.0
1989/90	250.8	167.5	81.4	132.8	32.5
1990/91	231.8	154.8	85.0	138.6	36.6
1991/92	353.0	235.8	104.3	170.2	29.5
Average 1982/92	237.64	158.7	84.2	137.4	35.4

Source: Compiled by the Author based on the field survey

**Table 2**  
**Composition of Receivables in BTMC During 1982--92**

Year	A/R (Crore TK)	Change over base year (percent)	O/R (Crore TK)	Change over Base year (percent)	T/R (Crore TK)	A/R as percent of T/R	O/R as percent of T/R
1982/83	21.5	100.0	39.8	100.0	61.3	35.1	64.9
1983/84	26.8	124.7	42.4	106.5	69.2	38.7	61.3
1984/85	34.0	158.1	42.0	105.5	76.0	44.7	55.7
1985/86	40.1	186.0	45.1	113.3	85.2	47.1	52.9
1986/87	51.9	241.4	50.4	126.6	102.3	50.7	49.3
1987/88	16.9	78.6	74.6	187.4	91.5	18.5	81.5
1988/89	17.5	81.4	68.4	171.9	85.9	20.4	79.6
1989/90	11.9	55.3	69.5	174.6	81.4	14.6	85.4
1990/91	9.4	43.7	75.5	189.7	85.0	11.0	88.8
1991/92	12.1	56.3	92.2	231.7	104.3	11.6	88.4
Average 1982/92	24.2	112.6	60.0	150.8	84.2	28.7	71.3

Note: A/R = Accounts Receivable, O/R = Other Receivables, T/R = Total Receivables.

Source: As of Table 1



**Table 3**  
**Turnover and Average Collection Period of Total Receivables (T/R),**  
**and Accounts Receivable (A/R) in BTMC During 1982--92**

Year	Avg. T/R (Crore TK)	Avg. A/R year (percent)	Total sales (Crore TK)	Turnover of T/R (Times)	Average Collection Period of T/R (Days)	Turnover of A/R (Times)	Average Collection Period of A/R (Days)
1982/83	65.1	19.6	255.3	3.9	93	13.1	28
1983/84	65.2	24.2	298.9	4.6	79	12.4	29
1984/85	72.6	30.4	272.0	3.7	98	8.9	41
1985/86	80.6	37.0	290.6	3.6	101	7.9	46
1986/87	93.7	46.0	282.3	3.0	121	6.1	60
1987/88	96.9	34.4	340.5	3.5	104	9.9	37
1988/89	88.7	17.2	372.9	4.2	87	21.2	17
1989/90	83.6	14.7	404.6	4.8	76	27.5	13
1990/91	83.2	10.6	417.1	5.0	73	39.3	9
1991/92	94.6	10.8	317.5	3.4	107	29.4	12

Source: As of Table 1

**Table 4**  
**Coefficient of Variation, Correlation, and Calculated 't'-value**

Variable	Total No. of years	CV percent	Correlation	't'-value
<b>Current Assets and Total Receivables</b>				
C/A	10	22	0.706	2.818
T/R	10	16		
<b>Total Receivables of Other Receivables</b>				
C/A	10	16	0.651	2.426
T/R	10	30		
<b>Total Receivables and Accounts Receivable</b>				
T/R	10	16	0.434	1.362
A/R	10	57		
<b>Net Sales of Accounts Receivable</b>				
N/S	10	17	-0.681	-2.632
T/R	10	57		

Surce : As of table 1

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