

## LIQUIDITY AND PROFITABILITY ANALYSIS OF HOTEL COMPANIES

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### ABSTRACT

*The liquidity and profitability of Government and private hotel companies showed fluctuating trend and often found inefficient. Although private hotel companies have been found more liquidity conscious in comparison to Government hotel companies but overall, none of them observed in a secure and efficient liquidity position to overcome its liabilities in time. One possible reason for industrial sickness is the poor management of liquidity. A firm in order to remain in existence and sustain its activities as an ongoing concern must had enough liquidity to meet its obligations as and when they become due. And, analysis showed that hotel companies under study showed a mixed profitability condition and no one is best or worst performer.*

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**Keywords:** *Liquidity, Profitability, Liquid Ratio, Return on Equity and Return on Capital Employed.*

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### Introduction

#### Liquidity

For a business organization, availability of short-term fund in most liquid form is very important. The small, but very important short-term transactions need availability of sufficient liquid resources. Short-term solvency much depends upon the availability of liquid resources as per short-term requirements. No businessman can aspire to keep surplus fund in the business but while developing these surplus funds, he/she has to estimate its short-term requirements. Liquidity effects over short-term capacity to pay day to day, say routine transactions.

Thus, the businessman wants to hold imbalance, a sufficient quantity of liquid assets. So that undue solvency risks are not imposed on it. This is a logical approach indicating quantitative amount of liquid resources. Thus, in the modern business atmosphere, financial experts have to consider a minimum amount of liquid capacity in the business appraises management in estimating property that prospects needs. Insufficient liquid resources may cost a black shadow on goodwill of the concern because the ability to pay short-term liability may be doubted by the external parties. Thus, the concept of liquidity comes in the light of proper financial functioning to the business.

In accounting and financial analysis, a company's liquidity is a measure of how easily it can meet its short-term financial obligations.

High liquidity means an asset can be easily converted to cash for the expected value or market price. Low liquidity means that markets have few opportunities to buy and sell, and assets become difficult to trade. The liquidity of an asset can also refer to how quickly it can be converted to cash

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because cash is the most liquid asset of all. One can calculate a company or person's liquidity position through ratio analysis, which compares an entity's assets against their liabilities. An entity is solvent if their total assets are higher than their liabilities, meaning that they can pay their debts and still have working capital left over.

### Types of Liquidity

There are three types of liquidity. Here is a brief overview of these types:

- **Asset Liquidity**

The liquidity of an asset refers to how easily that asset can be converted to cash when it is bought or sold. Cash is the highest liquidity asset because it can be traded easily and quickly without any effect on its market value. Stocks and bonds are also considered highly liquid assets, although their liquidity can vary depending on the popularity and reliability of the stock. Examples of illiquid assets include real estate and high art, as although they're highly prized they can be more difficult to sell and their price fluctuates with the market.

- **Market Liquidity**

Market liquidity refers to the conditions of a market in which an asset can be bought or sold. If market conditions support a high number of buyers and sellers, the market has high liquidity because it is easier to buy or sell assets at the desired price. Illiquid markets are financial markets in which there are fewer buyers or sellers for example, the market for rare collectibles which makes it harder to sell assets at desired price. During periods of financial crisis, stock markets become less liquid.

- **Accounting Liquidity**

Accounting liquidity refers to a company's ability to pay off financial obligations such as marketable securities, cash, inventory, and accounts receivable. Investors looking at a company's stocks often consider the company's accounting liquidity, because this can convey the state of a company's financial health.

### Profitability

Operational and financial efficiencies, both are the result of profitability. All business activities are done with keep in mind of profitability. Measurement of profitability is not small concept, it is a multi-stage concept. An important meaning to profitability has been given by Hingorani, Ramanathan and Grewal in these words, "A measure of profitability is the overall measure of efficiency".

Profitability is a concept based on profits but since it is a relative concept, profits are to be expressed in relation to some other variables. Several ratios can be computed to measure the extent of profitability in quantitative terms. Profitability ratios are calculated to measure the operating efficiency of an enterprise. Profits can be related mainly to sales and investment to determine profitability.

An enterprise should be able to generate adequate profit on each rupee in sales. If sufficient profits are not generated through sales, it becomes problematic for an enterprise to cover its operating costs and the interest burden.

### Tools and Technique to Measure Liquidity and Profitability

Ratio analysis is a series of equations that calculate the solvency of a company or individual by comparing their assets against their liabilities and profitability by comparing their income or sales against expenditures and operating expenses.

Companies use liquidity and profitability ratios to gauge their liquidity, profitability and measure their current financial health. Here is a brief overview of some important ratios to measure liquidity and profitability.

- **Liquid Ratio**

The liquid ratio takes higher liquidity assets into account than the current ratio does. This ratio considers a company's cash and cash equivalents, short-term investments, and accounts payable against their current liabilities. Here is the formula to calculate the liquid ratio:

$$\text{Liquid Ratio} = (\text{Cash and cash equivalents, accounts payable, short-term investments}) / \text{Current Liabilities}$$

This is similar to the current ratio but only considers accounts receivable, cash, and bonds/stocks as assets. The liquid ratio is considered a more conservative measure of liquidity and is more applicable to businesses involved in retailing, wholesaling or manufacturing. To determine liquid

ratio, subtract inventory from company's current assets, then divide the result by its current liabilities. A liquid ratio of 1 or higher is considered optimal because it means the company can meet its current liabilities from assets on hand without having to sell off any inventory.

The liquid ratio of the hotel companies under study has been calculated and presented in the following Table 1.

**Table 1: Liquid Ratio of Hotels under Study**

(Ratio in times)

Year	Hotel Ashok	Hotel Samrat	Hotel Taj	Hotel Sheraton
2016-17	1.73	1.67	0.44	4.08
2017-18	1.63	1.56	0.65	63.94
2018-19	1.78	1.71	0.56	21.36
2019-20	1.87	1.80	0.48	70.67
2020-21	1.92	1.87	0.43	30.55
Average	1.79	1.72	0.51	38.12
S.D.	0.11	0.12	0.09	28.39
C.V. (%)	6.42	6.94	18.08	74.47

Source: Annual Reports and Accounts of the Hotel Companies under study from 2016-17 to 2020-21.

From Table 1, it can be observed that both Indian Tourist Development Corporation's hotels having liquid ratio more than 1.5 times throughout the period under study from 2016-17 to 2020-21 which is quite satisfactory. Standard deviation and coefficient of variation of the ratio of these Government hotels also remained very low which indicate minor fluctuations in the ratio in this period. On the other hand, liquid ratio for Hotel Taj showed a fluctuating trend and the average ratio was 0.51 percent which is unsatisfactory and indicates that Hotel Company faced difficulties to overcome its liabilities with this ratio. Contrarily, liquid ratio of Hotel Sheraton remained exceptionally high during the period under study averaged 152.33 percent which indicate a big amount of unutilised cash the Hotel Company having that should be used in a purposeful way.

- **Return on Equity Ratio**

Equity shareholders are the real owners of the company who bears all the risk, participate in management and are entitled to the profits remaining after all outside claims including preference share dividend.

Return on equity shareholders fund establishes relationship between profit available for equity shareholders and equity shareholders fund. This ratio indicates as to how well the funds of the owners have been used by the firm. This ratio examines whether the firm has been able to earn satisfactory return for the owners or not. Therefore, the owners/shareholders of the company are most interested to judge the profitability through ROE analysis. This ratio is calculated by dividing the profits available for shareholders by the shareholders fund. Expresses as a formula, the ratio is

$$\text{Return on Equity Shareholders Fund} = (\text{Net Profit after Tax} - \text{Pref. Shares Dividend}) / (\text{Equity Shareholders' Fund})$$

This ratio is the best measure of a company's profit earning capacity. It provides adequate test to evaluate whether a company has earned satisfactory returns for its equity shareholders or not.

The ratio of return on equity of the hotel companies under study has been calculated and presented in the following Table 2.

**Table 2: Return on Equity Ratio of Hotels under Study**

(Ratio in Percentage)

Year	Hotel Ashok	Hotel Samrat	Hotel Taj Palace	Hotel Sheraton
2016-17	3.45	8.15	5.17	2.41
2017-18	5.35	0.15	3.36	5.44
2018-19	11.85	6.27	5.88	7.95
2019-20	6.48	6.40	8.75	1.43
2020-21	-8.49	-8.64	-12.46	0.23
Average ( $\bar{X}$ )	3.73	2.47	2.14	3.49
Standard deviation ( $\sigma$ )	7.51	6.91	8.39	3.15
Coefficient of variation ( $\frac{\sigma}{\bar{X}} \times 100$ )	201.42	280.19	392.01	90.25

Table 2 shows that average return on equity ratio was highest i.e., 3.73 percent for Hotel Ashok followed by 3.49 percent of Hotel Sheraton, 2.47 percent of Hotel Samrat and lowest 2.14 percent for Hotel Taj Palace. From this analysis, it can be concluded that shareholders of Hotel Ashok received maximum return on their equity whereas Hotel Taj Palace's shareholders got minimum during the period under study. Hotel Sheraton had lowest standard deviation as well as lowest coefficient of variation. It indicates minimum fluctuations among the hotels under study which is quite satisfactory condition of the concern and should be maintained in future.

**F-test and ANOVA Table: Return on Equity Ratio**

To test whether the difference in the return on equity ratio of the selected hotel companies under study is significant or not, following hypotheses have been used:

- **Null Hypothesis (H<sub>01</sub>):** There is no significant difference in the return on equity ratio of the hotel companies under study (Inter Hotels).
- **Null Hypothesis (H<sub>02</sub>):** There is no significant difference in the year-wise return on equity ratio of the hotel companies under study (Intra Hotels).

**Table 3: ANOVA Table: Return on Equity Ratio**

Source	Sum	Degree of Freedom (d.f.)	Variance (Sum/df)	F-Ratio
(Between Companies) SSC	59.13	(c-1)=(4-1)=3	19.71	F=3.16 (between Companies)
(Within Companies) SSR	27.16	(r-1)=(5-1)=4	6.79	F=9.16 (within companies)
Error (SSE)	746.68	(c-1)(r-1)=12	62.22	

▪ **Inter-Company F-Test**

$$F = 62.22 / 19.71 = 3.16$$

Critical Value of F at 0.05 level of significance ( $V_1=12$  &  $V_2=3$ ) = 8.7446

**Inference:** From this analysis of ANOVA table, calculated value of F is less than the critical value of F. Therefore, null hypothesis is accepted and it can be concluded that there is no significant difference in the return on equity ratio among the hotel companies under study.

▪ **Intra-Company F-Test**

$$F = 62.22 / 6.79 = 9.16$$

Critical Value of F at 0.05 level of significance ( $V_1=12$  &  $V_2=4$ ) = 5.9117

**Inference:** From this intra-company analysis of ANOVA table, calculated value of F is more than the critical value of F. Therefore, null hypothesis is rejected and it can be concluded that there is a significant difference in the year-wise return on equity ratio of the hotel companies under study.

• **Return on Capital Employed**

The return on capital employed establishes relationship between capital employed and net profit of a concern. This ratio is similar to return on assets, the only difference is that here profits are taken as percentage of capital employed. By capital employed means long term funds which are provided by money lenders and owners of the business. Capital employed can be calculated by two ways: Firstly, it is equal to the total of non-current liabilities (Long term liabilities) and owners' equity. Alternatively, it is equal to the total of net working capital and fixed assets. In this way, on the basis of capital employed, profitability in relation to long term funds can be tested.

$$\text{Return on Capital Employed} = [(\text{Profit or EBIT}) / (\text{Capital Employed})] * 100$$

The ratio of return on capital employed of the hotel companies under study has been calculated and presented in the following Table 3.

**Table 3: Return on Capital Employed Ratio of Hotels under Study**

(Ratio in Percentage)

Year	Hotel Ashok	Hotel Samrat	Hotel Taj Palace	Hotel Sheraton
2016-17	11.96	9.31	9.98	2.30
2017-18	4.14	1.49	8.69	5.44
2018-19	12.65	9.99	11.34	7.95
2019-20	12.61	10.05	10.99	1.43
2020-21	-6.80	-9.45	-3.08	0.31
Average ( $\bar{X}$ )	6.91	4.28	7.58	3.49
Standard deviation ( $\sigma$ )	8.46	8.48	6.05	3.14
Coefficient of variation ( $\frac{\sigma}{\bar{X}} \times 100$ )	122.46	198.17	79.77	90.11

Source : Annual Reports and Accounts of the Hotel Companies under study for the period from 2016-17 to 2020-21.

Table 3 shows that average return on capital employed ratio was highest i.e., 7.58 percent for Hotel Taj Palace followed by 6.91 percent of Hotel Ashok, 4.28 percent of Hotel Samrat and lowest 3.49 percent for Hotel Sheraton. From this analysis, it can be concluded that Hotel Taj Palace received maximum return on their capital employed whereas Hotel Sheraton got minimum return on capital employed during the period under study.

Hotel Sheraton had lowest standard deviation and lowest coefficient of variation as well indicating moderate fluctuations which is a satisfactory condition of the concern and should be maintained in future.

**F-test and ANOVA Table: Return on Capital Employed Ratio**

To test whether the difference in the return on capital employed ratio of the selected hotel companies under study is significant or not, following hypotheses have been used:

- **Null Hypothesis (H01):** There is no significant difference in the return on capital employed ratio of the hotel companies under study (Inter Hotels).
- **Null Hypothesis (H02):** There is no significant difference in the year-wise return on equity ratio of the hotel companies under study (Intra Hotels).

**Table 4: ANOVA Table: Return on Capital Employed Ratio**

Source	Sum	Degree of Freedom (d.f.)	Variance (Sum/df)	F-Ratio
(Between Companies) SSC	111.30	(c-1)=(4-1)=3	37.10	F=15.59 (between Companies)
(Within Companies) SSR	27.57	(r-1)=(5-1)=4	6.89	F=2.89 (within companies)
Error (SSE)	28.62	(c-1)(r-1)=12	2.38	

▪ **Inter-Company F-Test**

$F = 37.10 / 2.38 = 15.59$

Critical Value of F at 0.05 level of significance ( $V_1=3$  &  $V_2=12$ ) = 3.4903

**Inference:** From this analysis of ANOVA table, calculated value of F is more than the critical value of F. Therefore, null hypothesis is rejected and it can be concluded that there is a significant difference in the return on capital employed ratio among the hotel companies under study.

▪ **Intra-Company F-Test**

$F = 6.89 / 2.89 = 2.89$

Critical Value of F at 0.05 level of significance ( $V_1=4$  &  $V_2=12$ ) = 3.2592

**Inference:** From this intra-company analysis of ANOVA table, calculated value of F is more less the critical value of F. Therefore, null hypothesis is accepted and it can be concluded that there is no significant difference in the year-wise return on equity ratio of the hotel companies under study.

**Conclusion**

The liquid ratio analysis of the Hotel Companies under study showed that there is a significant difference in the liquidity management of Government and Private Hotel Companies. The Government Hotel Companies look more conscious and maintained both ratios adequate during the period under study but one of the Private Hotel Company (Hotel Taj) showed lower level of the ratio whereas other one (Hotel Sheraton) having exceptionally high amount of cash with it which is idle money. Hence, it can be concluded that liquidity management should be proper in all these companies.

From F-test analysis, significant difference was found in return on equity ratio whereas no significant difference was found in return on capital employed ratio in Government and private hotel companies (inter-company). Hence, it can be concluded that hotel companies under study showed a mixed profitability condition and no one is best or worst performer.

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