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MEASURING RELATION BETWEEN LIQUIDITY AND PROFITABILITY: A CASE OF HDFC HOUSING FINANCE

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ABSTRACT

Liquidity refers to the ability of the entity to pay its debts. It is typically measured by the company's total working capital, which is the balance of existing assets over current liabilities. The term "profitability" applies to the surplus of sales over expenditures. They are so intertwined that cash flow from financial operations is an indicator of liquidity change. Profitability applies to the company's increase of margins; margins equate to revenue-cost; the higher the margins, the greater the company's profitability for the fiscal year. Profitability increases the company's cash reserves and development opportunities. Liquidity, on the other side, relates to the firm's capacity to satisfy short-term and long-term commitments that the company would pay in the long run and the actual component of liabilities in the short run. This paper measures the ratios predicting the profitability in the Public and Private NPFC in India by taking a sample of LIC and HDFC housing finance companies. The results from multiple regressions by SPSS software revealed that the ROCE in public company and Cash to total assets ratio in private sector NBFC predict their profitability.

Keywords: *LIQUIDITY, Profitability, SPSS, ROCE, NBFC.*

Introduction

The two main parameters for valuation of any business analysis are viability and liquidity, which are the two critical conditions for a company to have creditworthiness and an increasing market capital and market share. Profitability vs. liquidity must be thoroughly examined. In this post, we will attempt to explain the distinction and characteristics of the two in depth, as well as why these two metrics are relevant for a financial analyst.

The power of a company to service its obligations is referred to as its liquidity. Normally, it is measured by the company's total working capital, which is the balance of operating assets over existing liabilities. The term "profitability" applies to the surplus of sales over expenditures. They are so intertwined that cash flow from financial operations is an indicator of liquidity change. Profitability applies to the company's increase of margins; margins equate to revenue-cost; the higher the margins, the greater the company's profitability for the fiscal year. Profitability increases the company's cash reserves and development opportunities. Liquidity, on the other side, applies to the firm's capacity to fulfil short-term and long-term commitments that the company must compensate in the long run, as well as the actual portion of liabilities in the short run.

One of the main distinctions being that a prosperous business would not necessarily have to be liquid in essence unless the company has spent extensively. In the company's upcoming ventures, where receivables are due for a long period of time. This is a significant distinction that must be recognised when doing financial forecasts for any organisation. A business that is not solvent in existence will still go bankrupt in the short run due to a lack of cash in its hands, which is why the company requires operating capital to satisfy short-term obligations. Profitability is an indicator of market performance that indicates how good the firm does over time. It is not an indicator of how cash-rich the corporation is and cannot

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say the analyst the company's cash status. Liquidity, on the other side, teaches us of the firm's financial position; so much cash on the balance sheet often implies weak working capital control, since the company bears the opportunity expense of cash that is left unused on the balance sheet. Profitability is a company's financial success metric that appears in the income statement that is listed as Net profit in the profit and loss account. If the net profit figure is low, it means that the business is losing money during that time frame. Apart from capital, liquidity is found in the balance sheet on the current assets portion of every company's balance sheet, which contains marketable securities, prepaid expenditures, and inventories.

Profitability vs Liquidity are also essential for a business since they are both crucial aspects of a corporation. If the firm does not have enough cash on hand, working capital control will be thrown out the window, and the organisation would need to search for a working capital loan, which would raise the interest rate of the enterprise. Profitability is therefore essential since the business must investigate the reasons for poor profit growth and emphasis on cost savings.

Reviews of Literature

Chandrasekhar (2015)[i] explained that “since the start of the economic liberalization program in India in the early 1990s, the property market in the country has expanded significantly. While India was experiencing a real estate boom, it was not affected by a similar crisis to that experienced in the real estate finance and residential property market in the United States and Europe during the 2007-2008 period. Indeed, after a brief pause in the worst phase of the global financial crisis, property prices appear to be rising again. This guarantees an examination of the type of development that has hit the property market in the country. The problem in India is therefore not the type of crisis that affects the property market, but whether the risks of the type that triggered the property collapse in the US and elsewhere are also accumulating in India, although the market is now showing signs of robust growth”.

Barlindhaug (2016)[ii] revealed that “The deregulation of Norwegian real estate and credit markets in the 1980s laid the foundation for aggressive marketing and an intensification of the struggle for credit customers, and the banks have carried out poor credit assessments. Strong fiscal and monetary stimulus plans and government support for the financial sector in response to the financial crisis helped stabilize Norway's economic development during the recent global financial crisis”.

Growe, et.al., (2014)[iii] used using the predictive emphasis of fundamental analysis science, determinants to model improvements in bank profitability one year forward, in addition to many variables not previously considered.

Nagar & Rajan (2005)[iv] Using financial and nonfinancial indicators on price, service, consumer use, and customer loyalty, describe the central deposit intangible, a significant retail banking intangible reflecting a bank's relationships with its customers. We discover that the parameters do not forecast potential earnings individually, but acquire individual importance in a group context, significantly enhancing the predictive capacity. They contend that this finding happens because the actions driving the interventions are causally related to earnings, and they use a systemic road model to directly demonstrate these linkages. Our calculation model often forecasts major interactive results in the way our measures inform about potential earnings, and we log such effects not just among individual measures, but also through measures and environmental variables such as the bank's strategy. To summarise, our assessment model depicts the core factors, metrics, and experiences in retail banking consumer relationships.

Ball et.al.,(2016)[v] revealed that cash-based operating profitability (a metric that removes accruals) outperforms accrual-based profitability measures Furthermore, in forecasting the cross section of average returns, cash-based operational profitability takes precedence over accruals. By applying only a cash-based operational profitability component to the investment incentive package, an investor will maximise the Sharpe ratio of a policy rather than by adding both an accruals factor and a profitability factor that requires accruals.

Plotnikova, Tumanov and Zhelezova (2016)[vi] reviewed the past of Russian housing finance since the 1980s.” Prior to the dissolution of the USSR, the state had a monopoly on funding housing production, building, and upkeep, resulting in widespread housing scarcity and poor housing standards. Following that, funding structures failed, forcing building volumes to fall. This fall was partly offset by an increase in private housing development in villages and towns that was self financed or partially funded with consumer loans. In towns, direct expenditure by buyer households at the building level predominates. The establishment of the Agency for Housing Mortgage Lending has aided the growth of the mortgage industry. Although market processes such as mortgage lending and securitisation are becoming more prevalent, aspects of the socialist housing scheme, such as free replacement of substandard housing, exist. The government also expanded its participation in the housing sector by subsidising demand for housing and supplying infrastructure.

Hutchison, Pasricha and Singh (2012)[vii] The self-exciting threshold autoregressive (SETAR) approach was used to examine the efficacy of foreign capital controls in India over time by comparing regular return differentials in non-deliverable forward (NDF) markets. The paper provides a narrative of the history of capital controls in India and develops a new measure of capital account liberalisation based on average monthly adjustments in constraints on inflows and outflows. It identifies specific policy episodes by using de jure indexes of adjustments in restrictions on capital inflows and outflows, and it measures the de facto impact of restrictions by estimating variations from covered interest parity (CIP) using data from the three-month offshore no deliverable rupee forward market. The paper uses SETAR to approximate no-arbitrage bands for each episode, with the limits defined by transaction costs and the efficacy of capital controls. It discovers that Indian capital controls are asymmetric on inflows and outflows, that they transitioned from mainly restricting outflows to essentially restricting inflows at one stage, and that arbitrage operation closes deviations from CIP when the threshold thresholds are crossed in all sub-periods. Furthermore, the findings show a substantial decline in arbitrage barriers since 2009, implying that steady liberalisation of India's capital account has played a significant role in merging onshore and offshore markets. The technique is also applied to the Chinese RMB NDF industry, where it is discovered that capital restrictions are strictly controlling capital inflows with the exception of two cycles of regional and foreign financial volatility. The level of Chinese restrictions changes with time, reflecting discretion in capital control policy implementation, however, unlike India, there is no evidence of incremental easing or liberalisation.

Kenna (2016)[viii] revealed Market oriented housing initiatives in Ireland have long encouraged owner occupation in order to satisfy the housing needs of its increasingly industrialised and urbanised population. Thus, the affordability and accessibility of housing finance has been a major issue in Irish housing, especially over the last quarter-century. Housing financing was vital to the acceleration of production and manufacturing, credit expansion, increasing house prices, expanded family creation, and, most recently, a global financial crash and recession. Mortgage lending increased significantly between 2000 and 2007 as a consequence of financial reform liberalisation beginning in the late 1980s, lower interest rates, and increased access to foreign finance. This resulted in a huge property boom, perhaps the worst in the industrialised world, accompanied by the largest crash, not just of house prices by more than half, but also in Irish state finances. Today, the European Central Bank has instituted a new housing finance regulatory landscape, but in a sense in which all national lenders (except one) are nationalised. As the pace of new family development rises in a reasonably young demographic, there are signs of increased demand for both private and social rental accommodation, putting market strains on.

Cirman and Sendi (2016)[ix] decentralised the housing finance in Slovenia in 1991” Among other things, these laws, they ended the former status of the state as a main provider of accommodation. This is an overview of housing finance issues over the last quarter-century. we see the two primary players here (such as the National Housing Corporation and banks) and explain the ways in which these entities have impacted the housing market. We quickly summarise the long-term consequences of the Global Financial Crisis (Crisis) in the final section.

Mundt, A. and Springler, E. (2016)[x] revealed that in Austria, it was discovered that “tenure and financing are still dominated by housing rentals, especially by the cost of the latter Regional, low interest single family loans are the strongest position in the housing market. For promoting affordable housing, the Housing Banks are relied on to a significant extent to issue tax-exempt bonds. Single-family housing, mostly constructed by families, also relies on bequests and investments. To put it another way, the government's total housing debt to GDP ratio is modest, but it is growing. In the 2000s, FX loans from Japan and Switzerland were very common. Overall, the global financial crisis has a minor effect on Austrian housing finance. Resilience of external influences.

Research Methodology

- **Scope of Study:** The scope of the study is limited to HDFC Housing Development Finance companies.
- **Sampling:** The sample is the study is 1 NBFC’s stated above as they hold more than 35 percent of the housing finance market in India.

- **Population**: The housing finance sector is selected to conduct the current study, thus all housing finance companies are included in the universe of the current study.
- **Sample Unit:** Current study is limited to Housing Development Finance Corporation Limited (HDFC) working in private sector.
- **Sample Size:** The present study covers 1 NBFC's for a period of five years from 2014 to 2019.
- **Sampling Technique**: In present research, the companies were selected using convenience sampling (using a cross-sectional design) from private sector organisations.
- **Data Collection Method**: this study uses the secondary data of the 1 selected company taken from their official websites and research paper by online sources and online libraries.
- **Data Analysis Technique:** For the current research work Pearson correlation coefficient were used.

Data Analysis

The relation between the profitability and liquidity and its related items are subject to the growth of the company in a balancing way so that the company grow with adequate liquidity and also get the benefits of the liquidity. For this purpose the balance between the liquidity and profitability is measured with the Pearson coefficient of correlation between profitability and above mentioned factors was calculated. For HDFCHF the correlation is calculated as per table-1 as under:

Table 1: Correlation between liquidity and profitability in HDFCHF

Descriptive Statistics			
	Mean	Std. Deviation	N
NET_PROFIT	7163.0250	2637.84528	6
CR	.2700	.09633	6
QR	.2483	.08931	6
DEBTURN	325.6717	165.51476	6
CA2TA	.1200	.03950	6
CASHTURN	1.1067	.65031	6
ROCE	19.6017	.67822	6

Correlations								
		NET_PROFIT	CR	QR	DEBTURN	CA2TA	CASHTURN	ROCE
NET_PROFIT	Pearson Correlation	1	-.897*	-.908*	.009	-.936**	.925**	.204
	Sig. (2-tailed)		.015	.012	.986	.006	.008	.699
	N	6	6	6	6	6	6	6
CR	Pearson Correlation	-.897*	1	1.000**	-.242	.951**	-.937**	-.403
	Sig. (2-tailed)	.015		.000	.645	.003	.006	.429
	N	6	6	6	6	6	6	6
QR	Pearson Correlation	-.908*	1.000**	1	-.218	.958**	-.944**	-.393
	Sig. (2-tailed)	.012	.000		.678	.003	.005	.441
	N	6	6	6	6	6	6	6
DEBTURN	Pearson Correlation	.009	-.242	-.218	1	-.004	-.013	.081
	Sig. (2-tailed)	.986	.645	.678		.993	.981	.878
	N	6	6	6	6	6	6	6
CA2TA	Pearson Correlation	-.936**	.951**	.958**	-.004	1	-.998**	-.234
	Sig. (2-tailed)	.006	.003	.003	.993		.000	.656
	N	6	6	6	6	6	6	6
CASHTURN	Pearson Correlation	.925**	-.937**	-.944**	-.013	-.998**	1	.212
	Sig. (2-tailed)	.008	.006	.005	.981	.000		.687
	N	6	6	6	6	6	6	6
ROCE	Pearson Correlation	.204	-.403	-.393	.081	-.234	.212	1
	Sig. (2-tailed)	.699	.429	.441	.878	.656	.687	
	N	6	6	6	6	6	6	6
*. Correlation is significant at the 0.05 level (2-tailed).								
**. Correlation is significant at the 0.01 level (2-tailed).								

Pearson correlation of coefficient between the profitability and Current ratio, Quick ratio, Debtors turnover, current assets to total assets cash turnover and ROCE, a significant negative correlation were found for profitability and CR; r= -.897& p>0.05, QR= -.908& p>0.05, CA to TA=-.936& p>0.05 and positive correlation with cash turnover= .925 & p>0.05,

Conclusion

The relationship between the net profit and the selected ratios stating the current liquidity position, cash position and receivables position for each company and further for the selected company HDFCHF. As per table 1 the Pearson correlation of coefficient between the profitability and Current ratio, Quick ratio, Debtors turnover, current assets to total assets cash turnover and ROCE, a significant negative correlation were found for profitability and CR with positive correlation with cash turnover. The study results revealed that an imbalance between the profitability and these selected variables, thus the company needs to improve the same.

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