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## FINANCIAL ANALYSIS AND CASH MANAGEMENT

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### ABSTRACT

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*A comparative study of the quick ratio of all the companies under study focuses that the quick ratio in TKMCL TSMCL and TJWMCL were always less than the standard norm of which indicated that the quick assets available in the organization were not sufficient to meet its current obligations. But the quick ratio of ERWMC was always more than standard norm. Therefore, it is suggested that above three companies should try to improve their liquidity position and ERWMC should try to control their quick assets. To examine the liquidity position of selected textile companies of India and Jordan two methods have been applied such as current ratio and quick ratio. The current ratio was not overall satisfactory. The quick ratio is showing increasing trend, still the ratio is below the standard norm 1: 1. In the end it can be summarized that the liquid position of the selected textile mills should try to improve. This will be possible, if the inventory is reduced significantly and improve collection speedily and improve enough cash funds to meet the current obligations*

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**Keywords:** *Cash Management, Functions, Scope of Cash, Control of Cash Flows Sales Ratio, Current Liabilities, Operational Adequacy*

### INTRODUCTION

Textile Industry require a certain amount of cash to carry out their routine transactions. The amount of cash depends on the nature of the business activities. The amount of cash held also depends on the regularity of inflows (receipts) and outflows (disbursements). Industries that have highly predictable receipts and disbursements of funds can hold relatively less cash than firms that have irregular cash flows. For instance, the cash receipts of life insurance companies are highly predictable, and they hold upto one percent of their assets in the form of cash. On the other hand, the cash flows for aircraft manufactures are subject to wide variations, and they keep less than 8 percent of their assets in the form of cash.

#### **Precautionary Motive**

It is also related to the nature and level of business activity. Precautionary balances are those which are set aside because cash inflows and outflows are not synchronized. For instance, precautionary balances may be used to meet an unanticipated expense as the result of an unanticipated decline in sales revenues.

#### **Control of Cash Flows**

The main purpose of a concern is to maximize profitability and so it should employ liquid funds as much as possible, on the other hand, it should optimize cash holding without affecting the overall liquidity position of the firm. This can be achieved by keeping a tight control over cash flows. The concern can develop a pattern from past experience and compare the company's own cash balance with those of other concerns in the same group of industry to find out what portion of current assets should be kept as cash balances to maintain proper liquidity and avoid risk of holding excess cash balances in the business. The following ratios have been discussed in this regard for selected textile mills in India and Jordan.

- i) Cash to total Current Assets
- ii) Cash to Sales
- iii) Cash to Current Liabilities
- iv) Cash to Current Assets Ratio

The idle cash balance lying in a concern affects the profitability of that concern. In an inflationary condition, cash

losses it purchasing power over a period of time. This ratio, the greater may be the profitability of the concern. A down-ward trend in this ratio over a period of time indicates a high control of cash whereas an upward trend reveals lack of control over cash resources. It is very difficult to lay down any standard in this regard. The adequacy of cash in respect of other components can be judged only from past experience. However, in a comfortably financed business, it will probably run not less than 5 to 10 percent of the current assets. The ratio of current assets to current liabilities should be 2: 1 and cash percentage should be 10 to 20 percent of the current assets, sometimes debtors and cash taken together vis-a-vis the total current assets. "In such a case, it may be stated in a general way that cash and debtors together should be 50 percent and stock and other assets should be remaining 50 percent of the total current assets".

So cash and debtors are supposed to look after the requirements of textile industry operations as well as a part of current obligations, the other part would be met from inventory and other current assets. Table 4.2 given below shows the cash to current assets ratio in The Kohinoor Mills Co. Ltd. The Standard Mills Co. Ltd. Elzay Ready wear manufacturing Co. and The Jordan Worsted Mills Co. Ltd. are given in table 1.1

**Table 1.1 Cash to Current Assets Ratio (1999-2004) (In percentage)**

Year/Name of Companies	TKMCL	TXMCL	ERWMC	TJWMCL
1999	5.06	4.77	3.82	4.02
2000	4.15	6.33	1.50	5.62
2001	2.94	6.00	10.83	4.37
2002	4.38	8.15	7.49	5.89
2003	2.47	7.28	1.82	3.02
2004	4.61	12.56	28.91	5.79

*Source: Computed from Annual Reports and Accounts of identified textile industry in India & Jordan*

Table 1.1 signifies that the cash to current assets ratio in TKMCL has an fluctuating trend throughout the study period from 1999 to 2004 except in 2000, 2001 & 2003. It was 5.06 percent in 1999. Then it decreased to 4.15 percent in 2000. However, it again decreased to 2.94 percent in 2001, 4.38 percent in 2002 and came down to 2.47 percent in 2003. Lastly in the year 2004 it was 4.61 percent. The above analysis shows that the management of cash was best in the year 1999 whereas it was worst in the year 2003. This reflects that the profitability of the company was also good in the year 1999 in comparison to 2003.

Table 1.1 reveals that the ratio of cash to current assets in TSMCL 4.77 percent in 1999 increased to 6.33 percent in 2000 and 6.00 percent in 2001. It was 8.15 percent in 2002, reduced to 7.28 percent in 2003 and increased to 12.56 percent in 2004 which was the highest during the whole study period. The cash kept by the company was more than its requirements in the year 2004. This affected the profitability of the company adversely. So the management took corrective actions and reduced the cash position which added to the profitability of the company.

Table 1.1 shows that the ratio of cash to current assets in ERWMC was 3.82% in 1999 which decreased to 1.50% in 2000 and sharply increased to 10.83% in 2001. However, it again decreased to 7.49% in 2002 1,82% in 2003 and rose to 28.91 % in 2004.

Table 1.1 shows that the ratio of cash to current assets in TJWMCL was 4.02% in 1999 which increased to 5.62% in 2000 and again decreased to 4.37 in 2001. However it again increased 5.89 % in 2002, 3.02% in 2003 and sharply increased to 5.79% in 2004.

It can be observed from the above analysis that on the whole the percentage of this ratio in TSMCL was the highest as compared to TKMCL, TJWMCL and ERWMC. This on one hand, showed a sound liquid position and on the other, a huge amount of idle cash balance in the company which could have been profitability utilized. On the whole this ratio was minimum in the TKMCL which indicates better utilization of available cash to obtain maximum profit.

### Cash to Sales Ratio

This is also an important ratio of controlling cash in textile industry in India and Jordan. As Sangam observes that, "the increase in sales is generally associated with large bank balances". A study of cash to sales ratio will provide a deep insight into the cash balances held in the selected textile mills. The cash to sales ratio in TKMCL, TSMCL, ERWMC and TJWMCL of study from 1999 to 2004 has been presented in Table 1.2

**Table 1.2 Cash to Sales Ratio (1999-2004)**

Year/Name of Companies	TKMCL	TXMCL	ERWMC	TJWMCL
1999	3.65	2.82	4.06	3.60
2000	2.40	3.54	1.59	2.44
2001	1.73	3.04	7.32	1.90
2002	2.86	3.92	4.00	2.90
2003	2.06	3.92	1.06	2.42
2004	4.25	6.59	14.43	4.10

*(Source: Computed from Annual Reports and Accounts of identified textile industry in India & Jordan)*

It is evident from Table 1.2 that in TKMCL cash to sales ratio had a fluctuating trend throughout the period of study from 1999 to 2004. It was 3.65 percent in 1999 which came down to 2.40 percent in 2000 and 1.73 percent in 2001. However, it increased to 2.86 percent in 2002, 2.06 in 2003 and lastly in 2004 it was 4.25 percent. On the whole the company's position cannot be considered good from the liquidity point of view, so the company should try to increase this ratio.

It is clear from the above table that the ratio of cash to sales in TSMCL was the highest in 2004. It was 6.59 percent in the year 2004 in comparison to 2.82 percent in 1999, 3.54 percent in 2000, 3.04 percent in 2001, 3.92 percent in 2002 and 2003. As far as liquidity position of TSMCO is concerned it is better than TKMCL and it can be considered good.

It is clear from the table 4.3 that the ratio of cash to sales ERWMC was the highest in 2004. It was 14.43 percent this year in comparison to 4.06 percent in 1999 1.59 percent in 2000, 7.32 percent in 2001, 4.00 percent in 2002 and 1.06 percent in 2003.

It is evident from Table No. 1.2 that in TJWMC cash to sales ratio had a fluctuating trend throughout the period of study. It was the highest in 2004. It was 4.10 percent this year in comparison to 1.90 percent in 2001, 2.44 percent in 2000, 2.90 percent in 2002, and 2.42 percent in 2003.

It can be observed from the above analysis that on the whole the cash to sales ratio in ERWMC was the highest as compared to TKMCL TSMCL and TJWMCL. This, on the one hand indicated a sound liquidity position and on the other, shows that a significant portion of cash balances remained unused which the company could have used profitably. TKMCL & TJWMCL were enjoying the best position.

### Cash to Current Liabilities

This ratio is another way of looking at the effort of the company to control cash balances. It analysis the level of liquid resources in relation to current obligations. The cash position ratio in TKMCL, TSMCL, ERWMC & TJWMCL for the period of study from 1999 to 2004 has been presented in the Table 1.3

**Table 1.3 Cash Position Ratio (1999-2004) (In percentage)**

Year/Name of Companies	TKMCL	TXMCL	ERWMC	TJWMCL
1999	7.34	6.67	6.52	7.88
2000	5.30	9.67	2.77	5.89
2001	4.02	9.22	18.02	4.37
2002	7.43	14.50	20.61	7.37
2003	4.50	15.09	5.26	4.52
2004	10.12	25.03	48.93	10.57

*Source: Computed from Annual Reports and Accounts of identified textile industry in India & Jordan*

It is evident from the above table that the cash position ratio in TKMCL remained fluctuating throughout the period of study from 1999 to 2004. This ratio was 7.34 percent in 1999 and came down to 5.30 percent in 2000 and decreased to 4.02 percent in 2001, this was mainly due to sharply increase in current liabilities but the absolute amount of cash was decreased. It was again sharply increased to 7.43 percent in 2002, 4.50 percent in 2003 and 10.12 percent in 2004.

It is clear from the above table that the cash position ratio of TSMCL fluctuated from year to year. It was 6.67 percent in 1999, 9.67 percent in 2000, 9.22 percent in 2001, 14.50 percent in 2002, 15.09 percent in 2003 and 25.03 percent in 2004. On the whole the ratio in TSMCL was always more than the ratio in TKMCL. This indicates that the cash position of the company was satisfactory.

It is evident from the above table that the cash position in ERWMC remained fluctuating throughout the period of study from 1999 to 2004. This ratio was 6.52 percent in 1999 which decreased to 2.77 percent in 2000 and increase to 18.02 percent in 2001 mainly due to sharp increase in cash but the current liabilities was slightly increased. The ratio was 20.61 percent in 2002, 5.26 percent in 2003 and 48.93 percent in 2004. This indicates that cash position of the company was satisfactory.

It is evident from the table 4.4 that cash position ratio is TJWMCL remained fluctuating throughout the period of study from 1999 to 2004. This ratio was 7.88 percent in 1999 and came down to 5.89 percent in 2000 and decreased to 4.37 percent in 2001. It was again sharply increased to 7.37 percent in 2002, 4.52 percent in 2003 and 10.57 percent in 2004.

It can be concluded from the above analysis that the cash position in ERWMC was best as compared to the cash position in TKMCL and TSMCL. On the other hand, it also represented under utilization of liquid funds. In case of TKMCL and TJWMCL the cash position were not so good as compared to the cash position of the ER WMC, TSMCL. It reveals that very low amount of cash balance was kept by TKMCL and TJWMCL.

### Operational Adequacy of Cash

The level adequacy of cash differs from industry to industry and from firm to firm due to variations in the quantum of output, nature of demand, payment of wages and salaries, availability of credit and fluctuations in the

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### Operational Adequacy of Cash

The level adequacy of cash differs from industry to industry and from firm to firm due to variations in the quantum of output, nature of demand, payment of wages and salaries, availability of credit and fluctuations in the price of materials stores and spares etc. According to James E. Walter, "A business enterprise should keep its cash and near cash reserves below the requirements of one month's normal expenditure. If cash and near cash reserves happen to be more than this limit, it should be taken for granted that excessive cash is being kept by the firm". The actual position TKMCL, TSMCL, ERWMC and TJWMCL in this regard stood as shown in the table No. 5.5

**Table 1.3 Turnover of Cash and Cash in Number of Days (1999-2004)**

Year/Name of Companies	TKMCL	TSMCL	ERWMC	TJWMCL
1999	27.42 (13)	35.46 (10)	24.65 (15)	26.79 (12)
2000	41.62 (9)	28.23 (13)	62.80 (6)	40.62 (9)
2001	57.95 (6)	32.85 (11)	13.66 (27)	55.22 (6)
2002	60.23 (6)	35.23 (10)	25.01 (15)	61.79 (7)
2003	69.35 (5)	39.28 (9)	93.96 (4)	70.23 (5)
2004	70.23 (5)	42.23 (9)	6.93 (53)	72.89 (5)

Source: Computed from Annual Reports and Accounts of identified textile industry in India & Jordan

Note: Figures in parenthesis show the numbers of days for which the size of cash build was sufficient to finance the normal expenditure of the TKMCL, TSMCL, ERWMC and TJWMCL.

Table 1.4 signifies that the turnover of cash in TKMCL was on an increasing trend throughout the study period from 1999 to 2004. It was 27.42 times in 1999, 41.62 times in 2000, 57.95 times in 2001, 60.23 times in 2002, 69.35

times in 2003 and 70.23 times in 2004. The cash in number of days also registered a decreasing trend throughout the period covered by this study. It should be noted that there exists a revenue relations between the turnovers of cash in number of days. The cash in number of days was minimum at 5 days in 2003 and 2004 and highest at 13 days in 1999.

It is evident *from* Table 4.5 that the cash turnover ratio of TSMCL marked a increasing trend throughout the study period *from* 1999 to 2004 except in the 2000 year. The ratio was 35.46 times in 1999 which increased to 42.23 times in 2004.

It is evident *from* table 4.5 that the cash turnover ratio as well as a cash turnover in number of days in ERWMC marked a fluctuating trend throughout the study period *from* 1999 to 2004. The ratio was 24.65 times in 1999 which came down to 6.93 times in 2004.

It is evident *from* table 4.5 signifies that the turnover of cash in TJWMCL had an increasing trend throughout the study period *from* 1999 to 2004. It was 26.79 in 1999, 40.62 times in 2000, 55.22 times in 2001, 61.79 times in 2002, 70.23 times in 2003 and 72.89 times in 2004. The cash in number of day also registered a decreasing trend throughout the period covered by this study. The cash in number of days was minimum at 5 days in 2003 & 2004 highest at 12 days in 1999.

It can be observed from the above analysis that the turnover *of* cash in TKMCL and TJWMCL were very high as compared to the turnover *of* cash in TSMCL and ERWMC. A high turnover *of* cash may be considered good for the business but at the same time it should also be noted that a relatively high turnover ratio may not really be an indicator *of* better results as it may indicate a low level *of* cash build by the company. A very high turnover *of* cash shows that the concern has not made proper provisions for emergencies. In case *of* TSMCL, the turnover *of* cash was lowest as compared to TKMCL, ER WMC and TJWMCL. A low turnover *of* cash may reflect dull management *of* cash and high amount *of* cash held by the company. Therefore, it is suggested that all the companies.

#### **Cash Flow Statement:**

It gives clear picture *of* the causes *of* changes in the company's cash position and reveals the financing and investing policies followed by the company. The cash flow statement shows the manner in which fixed assets acquired by the textile industries has been financed by the internal and external sources. Since cash is the basis for carrying on operations, the statement prepared on an estimated basis for the next accounting period will enable the textile mills management to plan and co-ordinate the financial operations properly. The management will know how much funds are required and how much can be generated internally and how much should be arranged from external sources.

It shows (i) the inflows of cash (ii) outflows of cash and (Hi) net change in cash. The inflows of cash are the sources of working capital, changes within the working capital account and increase the cash resources of the business. The outflow of cash is in the utilization of working capital and charges within the working capital account will reflect the cash resources of the business. The basic objective of cash flow statement is to show from where the textile mills acquired cash resources and where it applied or used resources. This statement is to show designed to account for the change in cash.

Purpose of Cash Flow Statement in Textile Industry: The main purposes of cash flow statement are;

- A) To provide information on all financing and investing activities of a mill.
- B) To shows the financial resources provided for operations and other sources.
- C) To show the inflows of financial resources.

- D) To disclose the amount and causes of all other changes in financial position.  
Uses of Cash Flow Analysis in Textile Industry:  
The uses of the cash flow statement analysis are:
- i) Since it reveals the amount of cash inflow from operations, it will be helpful for internal management to consider the possibility of retiring a long-term debt and in planning replacement of plant and machinery.
  - ii) It is useful to management in preparing cash budgets.
  - iii) The statement prepared for a particular accounting year when compared with the budget already prepared for that year would indicate to what extent the resources of the firm were raised and applied according to plan.
  - iv) Since cash is needed for carrying on day to day operations of the textile mills business activities, a projection of cash position also analyses various activities generating cash in the textile mills.

### **Concept of a Liquidity**

Liquidity means the speed and convenience in which certain assets can be converted in cash “Liquidity implies convertibility of assets ultimately into cash in the course of normal business operations and the maintenance of a regular cash flow. A sound liquid position is of primary concern to management from the point of view of meeting current liabilities as and when they mature as well as for ensuring continuity of operation.”

Liquidity can be measured with the help of some financial ratios. Liquidity ratios measure the liquid position of an enterprise. They throw a flood of light on the strength, working capital and the solvency of the firm. They point out if it would be possible for the firm to honour its financial obligations as and when they mature. If they are compared with turn-over, they will indicate the presence of any over trading or under trading.

Analysis of Liquidity: Analysis of liquidity is useful for creditors as well as internal management of a business firm. To the former it indicates the chances of receiving payment well in time and credit worthiness of the firm. To the latter it may indicate the adequacy of working capital and to what extent the organizations has under or over invested its funds in manufacturing cycle.

“Technical solvency relates to the ability of a given business unit to meet its currently maturing obligations”. It is a special class of solvency defined by the time interval of one year. The measurement of this forms the core of liquidity analysis. The liquid position of selected textile companies of India & Jordan has been measured with the help of the following ratio:

- i) Current Ratio, and

### **Current Ratio**

It may be defined as the ratio of current assets to current liabilities. The term current assets generally refer to those assets which change in their form and substance in the normal course of business operation and are ultimately realized in cash during the course of a year. The current liabilities on the other hand are short-term obligations maturing within a year. These liabilities are normally paid out of the funds arising from the realization of the current assets. in the normal course of a year. As such the relationship of current assets and current liabilities is very significant.

In the normal course of a year. The current liabilities include the sundry creditors, bills payables, bank over-draft and other out standing expenses. The current assets are cash, bills receivables, sundry debtors, investments and stock finished goods etc. According to Foulke, “If a contingent liability for bills discounted also appears by way of a foot note in the balance sheet then this item is to be included in both current assets and current liabilities, when

calculating the current ratio. The reason is that this item will also affect the current ratio position.

According to Batty, J., “Because of its link with the working of the Current ratio is not un-naturally some times referred to as the working capital ratio. Indeed the ratio is a vital measure of working capital available at a particular time. This assumes that the working capital is defined as the excess of current assets over current liabilities. The ratio is calculated by dividing current assets with current liabilities. Expressed in a formula current ratio is:

$$= \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

The unit of expression may be either 'times' or 'proportion'. An ideal current ratio as accepted by many authorities is 2:1 which means the current assets should be twice the current liabilities. The quotient so obtained from the above formula should be compared with the accepted ideal ratio of 2: 1. If it is less than it, then it is obvious that the solvency or liquidity of the concern is questionable. If the ratio is larger one then it is a sign of in-efficiency. The under-lying idea behind the ideal ratio is that even if the current assets shrink by 50% due to depreciation, deflation or any other loss in their value the short-term creditors will get back their entire amount. Some times a much higher ratio than 2:1 may be very desirable where as at other times a ratio of less than 2: 1 may be very desirable. The size of ratio depends upon the type of business and circumstances existing at the time.

In determining the current ratio it is important that all current assets and current liabilities are properly valued. If current assets values are not correctly estimated in the balance-sheet current ratio may be unduly inflated or unnecessary reduced.

The object of ascertaining this ratio is to measure the extent to which the payments which are to be made in a year are honoured. It guides regarding the solvency of the concern. It will help in planning the future working capital decisions.

Current ratio is the relationship of current assets and current liabilities. The object of calculating this ratio is to estimate the financial sources of the textile industry in comparison to financial liabilities. It measures on one hand strength of working capital position of the textile industry and on the other hand it indicates the financial soundness of the textile industry. This will help in the working capital decision of the textile industry. The use of this ratio requires a great deal of caution. It is not to be regarded as a conclusive proof of solvency, there might be window dressing or the presence of mounting stocks creating scarcity of cash through depicting a good working capital ratio. For reference, a current ratio of 2: 1 is ideal ratio. However, since the amount of the working capital and the size of current ratio depend upon many internal and external factors, a standard current ratio cannot be designated as appropriate for all type of industry.

Therefore, as regards the textile industry with larger investment in fixed assets and a slower operating cycle, the current ratio may decrease or fall to 1.5:1 or around and sometimes a current ratio lower than 2:1 happens to be good as well. This ratio gives an idea of liquidity position and short term financial strength of enterprise. According to Schatte and Jensen. “The current assets along with current liabilities in form of the short run ability used as indicator of short-term financial position of the company”. In the words of Clements and Dyer, "It is important that short term assets meet short term liabilities. This ratio is a measure of safety, as a business is not sound unless it has sufficient liquidity to meet its obligations. The table 4.6 gives the current ratio position of selected textile companies of India and Jordan. The current ratio in the TKMCL, TSMCK, ERWMC and TJWMCL for the period of study from 1999 to 2004 is given in Table 5.6.



**Table 1.4 Current Ratio (1999-2004)**

Year/Name of Companies	TKMCL	TSMCL	ERWMC	TJWMCL
1999	1.45	1.40	2.05	1.75
2000	1.72	1.53	1.71	1.92
2001	1.55	1.54	2.90	1.70
2002	1.92	1.83	2.90	1.98
2003	2.27	2.07	2.30	1.90
2004	2.39	1.99	1.80	2.31

*Source: Computed from Annual Reports and Accounts of selected textile companies*

It is evident from Table 1.4 that in TKMCL the current ratio varying from .45 times in 1999 to 2.39 times in 2004 forming a range of 0.94 times. The current ratio in the company marked a fluctuating trend throughout the period covered by this study. The current assets available in the concern to payoff current liabilities were more than two

It is clear from the above table in ERWMC the current ratio fluctuated from year to year. It was 2.05 times in 1999 which decreased to 1.71 times in 2000. However, it again increased to 2.9 times in 2001 and 2002. It again decreased to 2.3 times in 2003 and 1.8 times in 2004. The current assets available in the concern to payoff current liabilities were more than two times during the period of study except in the year 2000 and 2004.

The current ratio in TJWMCL for the period of study from 1999 to 2004 as shown in Table 5.6 reveals a fluctuating trend. It fluctuated from 1.70 times in 2001 to 2.31 times in 2004 forming a range of 0.61 times. The current ratio was less than two times during the period of study except in the year 2004.

On the basis of analysis of current ratio, it can be concluded that the financial position of ERWMC was unsatisfactory as compared to TKMCL, TSMCK and TJWMCL. It can be mentioned here that a good current ratio works like an umbrella for creditors in rainy days but on the other hand it also shows mismanagement of liquid fund

## **SUMMARY**

Important ratio of controlling cash in textile industry in India and Jordan. As Sangam observes that, "the increase in sales is generally associated with large bank balances". A study of cash to sales ratio will provide a deep insight into the cash balances held in the selected textile mills. The cash to sales ratio in TKMCL, TSMCL, ERWMC and TJWMCL of study from 1999 to 2004 has been presented

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