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Torres Abad, Maria Fernanda; Tinoco Pesantez, Lisseth; Gutiérrez Jaramillo, Néstor Daniel

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Journal of business and entrepreneurial studies, vol. 6, núm. 1, 2022

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Disponible en: <https://www.redalyc.org/articulo.oa?id=573669776003>



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Impact of portfolio turnover levels on liquidity: A case study of a home appliance company

Impacto de los niveles de rotación de cartera en la liquidez:
Caso de estudio de empresa de electrodomésticos

Maria Fernanda Torres Abad ¹


mftorresa_est@utmachala.edu.ec

Universidad Técnica de Machala, Ecuador

 <https://orcid.org/0000-0001-8392-015X>

Lisbeth Tinoco Pesantez ² ltinoco2@utmachala.edu.ec


Universidad Técnica de Machala, Ecuador

 <https://orcid.org/0000-0003-3214-2436>

Néstor Daniel Gutiérrez Jaramillo ³

ngutierrez@utmachala.edu.ec

Universidad Técnica de Machala, Ecuador

 <https://orcid.org/0000-0001-9487-6342>

Journal of business and entrepreneurial studies, vol. 6, núm. 1, 2022

Universidad de Oriente, México

Recepción: 14 Marzo 2021

Aprobación: 19 Junio 2021

Redalyc: <https://www.redalyc.org/articulo.oa?id=573669776003>

Abstract: This article is focused on the analysis of the financial ratios during the years 2018 and 2019 of Marcimex S.A., considered the largest home appliance trader in the country, with the purpose of establishing the variation that exists in the recovery of the portfolio from one year to another, in order to know if the current situation of the company is adequate. The research methodology developed is of inductive - deductive type by means of instruments such as direct observation, of longitudinal type where the results analyze reflect variation between the years 2018 - 2019; it is important to review its financial statements in order to verify the real and current situation of the company, applying the financial indexes: Liquidity, Portfolio Turnover and Leverage. It is possible to distinguish a significant percentage in the collection of accounts receivable in 2018, however, 2019 reflects a year with greater demand and variation of products. New strategies are proposed to provide encouraging results within the credit and collection area of this institution with the purpose of improving the client portfolio without affecting the commercial relationship.

Keywords: Accounts receivable, Portfolio recovery, Liquidity Leverage.

Resumen: El presente artículo se encuentra enfocado en el análisis de las razones financieras durante los años 2018 y 2019 de la comercializadora de electrodomésticos considerada la más grande del país Marcimex S.A. Con el propósito de establecer la variación que existe en la recuperación de cartera entre un año a otro, con el fin de conocer si la situación actual de la empresa es la adecuada. La metodología de investigación desarrollada es de tipo inductiva – deductiva por medio de instrumentos como la observación directa, de tipo longitudinal donde los resultados analizar reflejan variación entre los años 2018 – 2019; resulta importante revisar sus estados financieros con el fin de comprobar la situación real y actual de la empresa, aplicando los índices financieros: Liquidez, Rotación de cartera y Apalancamiento. Se logra distinguir un significativo porcentaje en la recaudación de cuentas por cobrar en el año 2018, sin embargo, el 2019 refleja un año con mayor demanda y variación de productos. Se plantea nuevas estrategias que proporcionen resultados alentadores dentro del área de crédito y

cobranza de esta institución con el propósito de mejorar la cartera de clientes sin afectar la relación comercial.

Palabras clave: Cuentas por cobrar, Recuperación de cartera, Liquidez Apalancamiento.

INTRODUCTION

Financial management has long been considered of great importance for the proper management of economic activities within a company, as stated in the words of de Lourdes et al., (2017) "administrative and financial management allows the good development of each of the areas of the company and its resources, generating solvency and capacity for growth" p. 60; thus, with the passage of time, financial management has evolved and has become an essential tool for the development and execution of a financial analysis.

"Financial analysis is mainly based on the calculation of indicators that reflect the liquidity, solvency, operating efficiency, indebtedness, performance and profitability of an entity. A company with liquidity is considered solvent but not always a solvent company obtains liquidity" (Roig & Soriano, 2015, p. 400)

The above leads us to consider the execution of a financial analysis within the present study project, taking as main tools the financial ratios, in order to perform a comparative analysis in the collection of portfolio within the commercial sector during the years 2018 - 2019.

Currently, every company that seeks to remain in the market chooses credit sales as a strategy, so it is essential to have a proper control of the receivable portfolio and the time it takes to recover it, those who form the organization must establish policies and procedures to ensure careful control of the account to avoid possible risks. (Villano, 2013, p. 420)

Most Ecuadorian commercial companies, in an attempt to increase sales, opt to offer more credit facilities to their clients, although this strategy represents higher sales and also presents a high risk by omitting important aspects that guarantee timely payment of the debt.

It is a real challenge for appliance marketers to keep up when granting credit to people with a high level of indebtedness because it is very likely that they will not be able to keep up with each and every one of their commercial obligations, directly affecting their cash flow.

The main problematic situation lies in the management of accounts receivable since they are considered a main element in the maximization of its equity, according to (Santelices & Santelices, 2017) "An optimal management of working capital provides a margin of safety, at the time when the company has the ability to self-generate cash for the financing of its operations thus generating a reduction in business risk" (p. 200), the current situation makes it possible that a crisis within the credit area may arise, therefore during the development of this research the financial information, liquidity, portfolio turnover and leverage will be analyzed to perform the proper collection strategies, ensuring optimal management of the customer portfolio.

Melgarejo et al., (2014) states: "In today's business environment, organizations have to be profitable, sustainable and competitive, and to achieve this, good management must be maintained" (p. 80).

That is why within the financial administration we can find the indicators or ratios that are an instrument to help the administration of the companies to solve problems and examine if there have been improvements from one year to another, adopting the best decisions that will benefit the entity. In its publication Vélez et al., (2019) states that financial statements show a structured idea of the financial situation of a company within a given time period, where their purpose is to provide information on the position of the entity, the results of its activities and the sources useful in the decision-making process. (p. 21)

Currently, "standards established through Financial Reporting Standards (FRS) are used for the presentation of information in relation to balance sheets in order to provide details of the current situation of a company for decision making" (Molina-Morales & Expósito-Langa, 2013, p. 111). Performing an analysis of the financial statements is extremely important since it could prevent problems and take advantage of opportunities that arise thanks to the accounting information. According to (Roig & Soriano, 2015) "Significance is determined by the potential of the information or the omission of the information to influence economic decisions made by users of financial statements." (p. 99)

Giacomozzi et al., (2013) It is a financial document where the Assets, Liabilities and Equity are presented in an orderly and systematic manner at a given time. According to Giacomozzi et al., (2013) "the balance sheet is static it represents a summary of everything the company has, what it is owed, what it owes and what actually belongs to its owner or shareholders at a given date" (p. 211).

According to Elizalde (2019), the cash flow statement reports the movements and changes in cash and cash equivalents during a period, this information is favorable because it provides the necessary basis for assessing the company's ability to generate cash and its liquidity needs, for optimal economic decision making.

As he points out Vélez et al., (2019) financial knowledge can be defined as the domain that an entrepreneur must have in order to understand the information related to personal finances and business. Financial analysis is important for proper management in the decision making of a company, to detect future difficulties and thus predict the economic and financial situation by applying appropriate corrective measures to solve them.

According to Santelices & Santelices, (2017) the horizontal analysis is performed to compare the items of the accounting statements in established periods of time and observe the trend of the values, i.e. how they increase or decrease. This analysis is performed integrally since each of the figures of the indicators do not represent a faithful result of the object of study, achieving the objective of contributing to improve decision making.

For López et al., (2017) who argues that the application of the analysis based on financial ratios corroborates and quantifies the effects detected in the horizontal and vertical analysis, with the opportunity to determine relationships in different financial issues and punctuate the real performance of the company. Financial tools are the key to business success by carrying out a decision-making process because they are a direct part of the economic stability of each company; also the efficient management of the tools helps to establish an accurate scenario where the current situation of micro, small and medium enterprises is analyzed, these financial strategies are used in order to increase the capacity of profits and income and obtain financial stability in the organization.

According to del Casasola (2015) these ratios reflect the capacity of a company to pay its liabilities in the short term; analyzing the degree of availability of the asset items and the degree of exigibility of the liability items by carrying out a relationship with each other.

The liquidity ratio is calculated based on the following formulas:

Table 1
Indicators

<i>Indicators</i>	<i>Formula</i>
<i>Current Ratio</i>	$= \frac{\text{Current Assets}}{\text{Current Liabilities}}$
<i>Acid Test</i>	$= \frac{\text{ACurrent Assets} - \text{Inventory}}{\text{Current Liabilities}}$

Source: Authors' elaboration

As he points out Rodríguez et al., (2015) these indicators also called turnover, try to measure the efficiency with which a company manages its assets according to the agility in the recovery of these values.

The activity ratio is calculated with respect to the following formulas:

Table 2
Activity ratio

Indiator	Formula
Inventory turnover	$= \frac{\text{Cost of Sales}}{\text{Average Inventory}}$
Portfolio Turnover	$= \frac{\text{Credit Sales in the period}}{\text{Accounts Receivable}}$
Collection Cycle	$= \frac{\text{Average Accounts Receivable} \times 365}{\text{Credit Sales}}$

Source: Authors' elaboration

According to Chicano, quoted by Casamayu (2019) indicates that "leveraging has innumerable advantages for the company, however, it is necessary to know how to use it and apply the appropriate level of leverage, taking into account that it is a recommended option where there is a certain risk of insolvency".

However, in order to determine the leverage, the debt ratios must be used, as they determine the proportion in which a company bases its financing with the help of third parties. de Oliveira & Abadía (2013) these determine the proportion in which a company bases its financing with the help of third parties.

The increase of debt in a company's financing structure or financial leverage has consequences on profitability, which depends on the financial cost of this debt.

Table 3
Leverage

Indicator	Formula
Debt Ratio	$= \frac{\text{Total Liabilities}}{\text{Total Assets}}$
AShort – term leverage	$= \frac{\text{Current Liabilities}}{\text{Heritage}}$

Source: Authors' elaboration

MATERIALS AND METHODS

The materials necessary for the development of this proposal is the information obtained from the company, among the most important could be mentioned the Statement of Financial Position from which data is collected from accounts of assets, liabilities, equity; the Income Statement where we find values of Sales, Cost of Sales; Cash Flows where the changes that cash has undergone during the periods 2018 and 2019 are evidenced providing the necessary foundation to evaluate its potential to generate cash; all these to be used for the calculation, comparison, analysis and interpretation of each of the financial ratios to be used.

The research methods used in this document are a non-experimental design, where the events and the context in which they develop in a natural way, i.e. the existing situations, are observed; each of the activities, collection policies, processes to provide credit to customers, current economic situation, longitudinal type that get information in different places of time, credit sales, portfolio recovery, inventory turnover and the collection cycle in the periods 2018 - 2019 were analyzed; the benefit of this method is that it allows the study and comparison of two causes, periods or situations.

The information examined for the analysis is supported by the financial statements of the commercial company that, through inductive-deductive research, where the observed environment is analyzed and verified, the control environment, information and communication, monitoring and follow-up of each of the credit sales granted, as well as the evaluation of possible risks and its response to them, it was possible to understand its current economic situation, the impact of portfolio recovery in relation to its liquidity, activity, leverage and its possible deficits in the follow-up of portfolio recovery.

In order to make known the reasonableness of the company's economy and to be able to determine coherent collection policies in view of the situation framing the sustainability of the company, as well as to give viable answers on the possible risk situations that may arise throughout its economic activity and thus maintain strong and sustainable business relationships with our customers and suppliers.

RESULTS

As for the analysis of the company Marcimex S.A., the company has a very significant solvency, which has helped it to remain in the market for many years, however, it should take the necessary corrective measures to put to work the money left over after covering all its debts.

With the above we can conclude that the company records as a result of acid test 0.79 and 0.81 in years 1 and 2 respectively, which means that for each dollar of debt assumed in the current liabilities it has \$0.79 and \$0.81 for its cancellation without the need to resort to inventories.

This indicator shows how many times the inventory rotates within a period, therefore, in 2018 inventories rotated 6.24 times in the year and in 2019 they rotated 6.69 times.

The company's portfolio recovery has decreased from one year to the next, however, it could be concluded that the result is acceptable since the expected indicator is 1, to be within acceptable parameters in the time it takes to recover the portfolio.

Taking into account the company's policies for granting loans to its customers, which range from 30 days to 24 months, the average period it takes the company to collect its debts is acceptable, considering the aforementioned.

For every dollar the company has in assets, it owes \$0.63 in 2018 and \$0.69 cents in 2019, i.e. transforming them to a percentage (63% - 69%) could be interpreted as the creditors' share of the company's assets.

From the point of view of the company's indebtedness, these results are good as long as the company achieves a positive result on profits, that is to say that the assets financed with debt generate a return for the company that exceeds the cost paid for the liabilities.

It can be deduced that the indicators applied during this study are important keys to determine the resources that the company has and meet its short-term obligations, because it is a company where its main source of income is credit sales, its liquidity index generated makes it positioned in a situation where at a given time is optimal, but it should be taken into account that this would be feasible in its entirety depending on the agility with which its inventories and portfolio are converted into cash.

From the perspective of Melgarejo et al., (2014) the financial indicators demand a process for the evaluation and issuance of a supported criterion, the realization of a comparison of historical values, to distinguish the evolution of the indicator, ideally two or more periods, it coincides with what was proposed above, since the results of the financial indicators were interpreted based on the use of the entity's resources; thus the comparison of the evolution, development and changes of the indicators during the chosen periods is also performed.

Similarly, our analysis, from a simple viewpoint, is coupled to most of the criteria issued by different authors, focusing on some comparisons and readings of basic results that offer a better interpretation helping managers and directors to assess the appropriate management that has been done with the company's assets, to take appropriate measures and improve future management.

CONCLUSIONS

Although the company has not shown complications in its collection of accounts receivable, the study of the financial ratios indicates that there is a slight delay in the payments made by its customers, it could be deduced that the defaults are due to the current economic situation, this study becomes an effective tool for making the necessary decisions. It is also proposed to take the necessary actions before the defaults advance to risk

levels, so it is suggested a process on credits and collections that performs a more effective analysis of each client in order to reduce the risk in portfolio recovery. Finally, it can be concluded that the impact of the portfolio rotation on the company's liquidity is basically an important complement due to the effectiveness with which it converts accounts receivable into cash and the opportunity to evaluate the credit policies offered by this entity.

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Notas de autor

- 1 Student of Accounting and Auditing at the Technical University of Machala, Machala, Ecuador mftorresa_est@utmachala.edu.ec, <https://orcid.org/0000-0001-8392-015X>
- 2 Student of the Accounting and Auditing Career of the Technical University of Machala, Machala, Ecuador ltinoco2@utmachala.edu.ec, <https://orcid.org/0000-0003-3214-2436>
- 3 Master's Degree, School of Business Sciences, Universidad Técnica de Machala, Machala, Ecuador ngutierrez@utmachala.edu.ec, <https://orcid.org/0000-0001-9487-6342>