A Study on Capital Budgeting At Sree Karpagam Organic Cotton Industries At Karur

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I. INTRODUCTION OF THE STUDY

Capital expenditure is an outlay of cash for a project that is expected to produce a cash inflow over a period of time exceeding one year. Examples of projects include investments in property, plant, and equipment, research and development projects, large advertising campaigns, or any other project that requires a capital expenditure and generates a future cash flow.

Because capital expenditures can be very large and have a significant impact on the financial performance of the firm, great importance is placed on project selection. This process is called capital budgeting.

CAPITAL BUDGETING – DEFINITION:

Capital budgeting (or investment appraisal) is the planning process used to determine whether a firm's long term investments such as new machinery, replacement machinery, new plants, new products, and research development projects are worth pursuing. It is budget for major capital, or investment, expenditures.

Many formal methods are used in capital budgeting, including the techniques such as

- Accounting rate of return
- Net present value
- Profitability index
- Internal rate of return
- Modified internal rate of return
- Equivalent annuity

These methods use the incremental cash flows from each potential investment, or *project* Techniques based on accounting earnings and accounting rules are sometimes used - though economists consider this to be improper - such as the *accounting rate of return*, and "return on investment." Simplified and hybrid methods are used as well, such as *payback period* and *discounted payback period*.

CONCEPT OF CAPITAL BUDGETING:

The term “capital budgeting” refers to long term planning for proposed capital outlays and their financing. Thus it includes both rising of long term funds as well as their utilization. It may thus be defined as “the firms formal process for the acquisition and investment of capital” .it is the decision making process by which the firms evaluates the purchase of major fixed assets. It involves firm’s decision to invest its current funds for addition, disposition, modification, and replacement of long term or fixed assets. However it should be noted that investment in fixed assets is also to be taken as a capital budgeting decision. Ex: A new distribution system may call for both new warehouse and an additional investment in investors. An investment proposal of this nature must be taken as capital budgeting decision evaluated as a single package but not as an investment in a fixed asset (i.e. warehouse) and in a current asset (investment) separately.

Capital budgeting is a many sided activity. It includes searching for DE 1:1 kind of more profitable investment proposals, investment engineering and marketing consideration to predict the consequence of accepting the investment and making economic analysis to determine the profit of each investment proposal.

- Its basic feature can be summarized as follows:
- It has potentially of making large anticipated profits.
- It involves a high degree of risk
- It involves a relatively long-term period between the initial outlay and the anticipated return..
- On the basis of the above discussions it can be concluded that capital budgeting consists in planning the development of available capital for the purpose of maximizing the long term profitability of the firm.

THE CAPITAL BUDGET EVALUATION PROCESS:

- Many companies follow a carefully prescribed process in capital budgeting. The process usually includes the following steps:
- Project proposals are requested from department’s plants and authorize capital budgeting. Capital expenditure is an outlay of cash for a project that is

expected to produce a cash flow over a period of time exceeding one year.

- Ex: Investments in property, plant, and equipment, research and development projects, large advertising company, or any other project that requires a capital expenditure and generates a future cash flow.
- Because capital expenditures can be very large and have a significant impact on the financial performance of the firm, great importance is placed on project selection. This process is capital budgeting.

II. REVIEW OF LITERATURE

1. **Prasanna Chandra (1975)** conducted a survey of twenty firms to examine the importance assigned to economic analysis of capital expenditures, methods used and its rationale for analyzing capital expenditures and ways to improve economic analysis of capital expenditures. The findings of the study reveal that the nature of economic analysis of capital expenditures varies from project to project but in most of the firms surveyed the analysis is done in sketchy terms. The most commonly used method for evaluating investments of small size is the PBP and for large size investments the ARR is used as the principal criterion and the PBP is used as a supplementary criterion.
2. **Pandey I M (1989)** In a study of the capital budgeting practices of fourteen medium to large size companies in India, it was found that all companies, except one, used payback. With payback and/or other techniques about two-thirds of companies used IRR and about two-fifths NPV. IRR was found to be the second most popular method. The reasons for the popularity of payback in order of significance were stated to be its simplicity to use and understand its emphasis on the early recovery of investment and focus on risk.
3. **Bennouna, K., G. Meredith, G., & Marchant, T. (2010).** Improved capital budgeting decision making: evidence from Canada. *Management Decision,48*(2), 225-247.In this article the authors tries to evaluate current techniques in capital budget decision making in Canada. They also figured out the fact that sound financial management and capital investment decision making are critical factors for survival and long-term success for firms. Our study also show that sound financial management lead to long-term success of the firm.
4. **Yasmin, S. (2015).** Capital Budgeting in Practice: An Explorative Study on Bangladeshi Companies. *International Journal of Engineering, Business and Enterprise Applications*,, 158-164. In her descriptive research she emphasizes on capital budgeting practices of the companies in Bangladesh. From the research it is evident that NPV and IRR are the dominating methods of capital budgeting. However Payback Period (PBP) is used by many of the companies. In our study, we try to figure out the dominating methods of capital budgeting and will focus on the other methods to show the actual practice of capital budgeting in Bangladeshi companies.

III. RESEARCH METHODOLOGY

The study of Capital Budgeting in**SREE KARPAGAM ORGANIC INDUSTRIES AT KARUR** has been carried out of studying the company's project reports, budget and revenue estimate. The study can broadly divided into two phase.

- Primary Data
- Secondary Data

Primary Data

The data which is collected at first had for the purpose of the study is known as primary data.

Primary data which is collected through interaction with the assistant financial manager of **SREE KARPAGAM ORGANIC COTTON INDUSTRIES AT KARUR**

Secondary Data

The data which is corrected by someone previously is called by . It is already available in the form of internal records of the company and other publications.

- Collecting relevant Annual Reports
- Analyzing the Collected data
- Drafting the report
- Updating the Final report

Collecting the general information about Capital Budgeting from various standard text books Studying the project report of **SREE KARPAGAM ORGANIC COTTON INDUSTRIES AT KARUR**

LIMITAIONS OF THE STUDY

- The topic for the study is very exhaustive and covers several crucial aspects of financial management for which the availabilities of the time is very much limited.
- Under the pretext of confidentiality the organization has not disclosed the total information.

- The study is made by secondary data collection and the calculation of various ratios depends on the information in the annual reports of the company.
- Through this study of the Capital Budgeting position in **SREE KARPAGAM ORGANIC COTTON INDUSTRIES AT KARUR** the sources of funds have affected a lot due to major fluctuation in the Capital Budgeting decision.
- The analysis made on the basis of secondary data
- The availability of data is only pertaining to four years is one of the constraints.
- As there is more dependency is secondary data realistic conclusion may not be possible to be made.
- Even though there are no if indicates for analyzing the financial performance the study includes about liquidity position.
- There may be approximations
- The study was carried in **SREE KARPAGAM ORGANIC COTTON INDUSTRIES AT KARUR** for a period of 8 weeks.

IV. FINDING, SUGESSTION AND CONCLUSION

- The current ratio has shown in a fluctuating trend as 7.41, 2.19, 4.48, 1.98, and 3.82 during 2012 of which indicates a continuous increase in both current assets and current liabilities.
- The quick ratio is also in a fluctuating trend throughout the period 2012-2017 resulting as 7.41, 1.65, 4.35, 1.9, and 3.81. The company's present liquidity position is satisfactory.
- The absolute liquid ratio has been decreased from 3.92 to 1.18, from 2012-2017.
- The proprietor ratio has shown a fluctuating trend. The proprietary ratio is increased compared with the last year. So, the long term solvency of the firm is increased.
- The working capital increased from 0.72 to 1.13 in the year 2012-2017.
- The fixed assets turnover ratio is in increasing trend from the year 2012-2017. (1.26, 1.82, 4.24, 3.69, and 6.82). It indicates that the company is efficiently utilizing the fixed assets.
- The capital turnover ratio is increased form 2012-2015017. (0.98, 1.01, and 1.04) and decreased in 2016 to 0.98. It increased in the current year as 1.00.
- The current assets to fixed assets ratio is increasing gradually from 2012-2017 as 2.93, 3.74, 4.20, 6.07 and 8.17. It shows that the current assets are increased than fixed assets.
- The net profit ratio is in fluctuation manner. It increased in the current year compared with the previous year from 2012-2017 0.33 to 0.42.
- The net profit is increased greater in the current year. So the return on total assets ratio is increased from 0.17 to 0.31.
- The Reserves and Surplus to Capital ratio is increased to 4.19 from 2.02. The capital is constant, but the reserves and surplus is increased in the current year.
- The earnings per share was very high in the year 2012 i.e., 101.56. That is decreased in the following years because number of equity shares are increased and the net profit is decreased. In the current year the net profit is increased due to the increase in operating and maintenance fee. So the earnings per share is increased.
- The operating profit ratio is in fluctuating manner as 0.99, 0.51, 0.41, 0.57 and 0.69 from 2012-2017respectively.
- Price Earnings ratio is reduced when compared with the last year. It is reduced from 3.09 to 2.39, because the earnings per share is increased.
- The return on investment is increased from 0.32 to 0.42 compared with the previous year. Both the profit and shareholders' funds increase cause an increase in the ratio

SUGGESTIONS

- Accurate position of the business cannot be estimated:
- It arises due to inflationary pressure and change in Government policies all these affect the budgeting performance.
- **NICORME LEATHER PROCESSING INDUSTRY AT CHENNAI** can carry out some promotional activities, so as to increase its sales and beat the competition
- Use of quarter Budget it leads to chances of improvement or modification.
- Quarter Budget helps industrial concerns to checks its actual performance. After ascertaining the actual performance if any modification requires that can be adjusted in next quarter.
- **NICORME LEATHER PROCESSING INDUSTRY AT CHENNAI** may appoint specialized and experienced finance manager to improve its finance performance.
- The company should have proper co-ordination between finance and marketing department.
- The company should have close watch on the market which helps to make new strategies.

CONCLUSION:

From the study it can be concluded that to know that budgetary control is treated as one of the better techniques for minimizing cost and maximizing profit in **NICORME LEATHER PROCESSING INDUSTRY AT CHENNAI**. Budgetary control technique Plays important role in the profit making or smooth running of the company

It co ordinates all the departments like Finance, Marketing, Production in the company. It makes the decentralization of authority in the organization which helps organization goal with in stipulated period of time. Budgetary control acts as safety for an organization because it helps to identify business risk and necessary steps can be taken to avoid the risk.

Budgetary control techniques help to know how the available monetary resources can be utilized effectively. This technique focus on efficiency in the allocation of resources in particular time. As the finance department is the soul of any organization. Budgetary control helps the organization by making finance department effectives

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