

ANALYSIS OF FINANCIAL RATIOS OF HINDUSTAN PETROLEUM CORPORATION LIMITED

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ABSTRACT

Hindustan Petroleum Corporation Limited (HPCL) is an Indian state-owned oil and natural gas company with its headquarters at Mumbai, Maharashtra and with Navratna status. HPCL has been ranked 260th in the Fortune Global 500 rankings of the world's biggest corporations (2013) and 4th among India's Companies for the year 2012. HPCL has about 25% marketing share in India among PSUs and a strong marketing infrastructure. The Government of India owns 51.11% shares in HPCL and others are distributed amongst financial institutes, public and other investors.

The oil and gas sector is among the six core industries in India and plays a major role in influencing decision making for all the other important sections of the economy.

In 1997-98, the exploration licensing policy(NELP) was envisaged to fill the ever increasing gap between India's gas demand and supply. A recent report points out the Indian oil and gas industries is anticipated to be worth US\$ 139.8 billion by 2015. India's economy growth is closely related to energy demand; therefore the need for oil and gas is projected to grow more, thereby making the sector quite conducive for investment.

Keywords: NELP, Navratns, HPCL, licensisng policy

1. INTRODUCTION

The Government of India has adopted several policies to fulfill the increasing demand. The government has allowed 100 percent foreign direct investment (FDI) in many segments of the sector, including natural gas, petroleum products, and refineries, among others. Today, it attracts both domestic and foreign investment, as attested by the presence of Reliance Industries Ltd. (RIL) and Cairn India. Backed by new oil fields, domestic oil output is anticipated to grow to 1 MBPD by FY16. With India developing gas-fired power stations, consumption is up more than 160 per cent since 1995. Gas consumption is likely to expand at a Compound Annual Growth Rate (CAGR) of 21 per cent during FY08–17. Presently, domestic production accounts for more than three-quarters of the country's total gas consumption. India is the fifth-largest Liquefied Natural Gas (LNG) importer after Japan, South Korea, the United Kingdom and Spain and accounts for 5.5 percent of the total global trade.

2. OBJECTIVE OF THE STUDY

- To evaluate the performance of the company by using ratios as a yardstick to measure the efficiency of the company.
- To understand the liquidity, profitability and efficiency positions of the company during the study period.
- To evaluate and analyze various facts of the financial performance of the company.
- To make comparisons between the ratios during different periods.
- To study the present financial system at HPCL.
- To determine the profitability, liquidity ratios.

Need for the study

- The study has great significance and provides benefits to various parties whom directly or indirectly interact with the company
- It is beneficial to management of the company by providing crystal clear picture regarding important aspects like liquidity, leverage, activity and profitability.
- The study is also beneficial to employees and offers motivation by showing how actively they are contributing for company's growth.
- The investors who are interested in investing the company's shares will also get benefited by going through the study and can easily take a decision whether to invest or not to invest in the company's shares.

3. RESEARCH METHODOLOGY

Research Methodology is a way to systematically solve research problems. It may be understood as a science of studying how research is done scientifically. So, the research methodology not only talks about the research methods but also considers the logic behind the method used in the context of the research study.

Research Design:

Descriptive research is used in the study because it will ensure the maximization of bias and maximization of reliability of data collected. The researcher had to use fact and information already available through financial statements of earlier years and analyze these to make critical evaluation of the available material. Hence by making the type of the research conducted to be both descriptive and analytical in nature.

From the study, the type of data to be collected and the procedure to be used for this purpose were decided.

Data Collection:

The required data for the study is basically secondary in nature and the data are collected from the audited reports of the company.

Secondary Data:

The sources of data are from the annual reports of the company from the year 2010-2011 to 2014-2015.

Ratio Analysis:

Financial Analysis is the process of identifying the financial strengths and weaknesses of the firm and establishing a relationship between the items of the balance sheet and profit and loss account.

Financial ratio analysis is the calculation and comparison of ratios, which are derived from the information in the company's financial statement. The level and historical trends of these ratios can be used to make inference about a company's financial condition, its operation and attractiveness as an investment. The information in the statement is used by

4. CLASSIFICATION OF RATIOS

Accounting Ratios are classified on the basis of the different parties interested in making use of the ratios. A very large number of accounting ratios are used for the purpose of determining the financial position of a concern for different purposes. Ratios may be broadly classified in to:

- (1) Classification of Ratios on the basis of Balance Sheet.
- (2) Classification of Ratios on the basis of Profit and Loss Account.
- (3) Classification of Ratios on the basis of Mixed Statement (or) Balance Sheet and Profit and Loss Account.

This classification further grouped in to:

- I. Liquidity Ratios
- II. Profitability Ratios
- III. Turnover Ratios
- IV. Solvency Ratios
- V. Overall Profitability Ratios

Classification of Ratios by Statement

- **On the basis of balance sheet**
 1. Current Ratio
 2. Liquid ratio
 3. Absolute liquid ratio
 4. Debt Equity Ratio
 5. Proprietary Ratio
 6. Capital Gearing Ratio
 7. Assets-Proprietorship Ratio
 8. Capital Inventory to Working Capital Ratio
 9. Ratio of Current Assets to Fixed Assets
- **On the basis of profit and loss account**
 1. Gross Profit
 2. Operating Ratio
 3. Operating profit ratio
 4. Net Profit Ratio
 5. Expense Ratio
 6. Interest Coverage Ratio

• **On the basis of profit and loss account and balance sheet**

1. Stock Turnover Ratio
2. Debtors Turnover Ratio
3. Payable Turnover Ratio
4. Fixed Asset Turnover Ratio
5. Return on Equity
6. Return on Shareholder's Fund
7. Return on Capital Employed
8. Capital Turnover Ratio
9. Working Capital Turnover Ratio
10. Return on Total Resources
11. Total Assets Turnover

12. LIQUIDITY RATIOS

13. (1) Current Ratio.
14. (2) Quick Ratio (or) Acid Test or Liquid Ratio.
15. (3) Absolute Liquid Ratio (or) Cash Position Ratio.

FINDINGS OF THE STUDY

16. (1) Current Ratio

17. Current Ratio establishes the relationship between current Assets and current Liabilities. It attempts to measure the ability of a firm to meet its current obligations. In order to compute this ratio, the following formula is used:
18. Current Ratio = Current assets/Current Liabilities
19. The two basic components of this ratio are current assets and current liabilities. Current asset normally means assets which can be easily converted in to cash within a year's time. On the other hand, current liabilities represent those liabilities which are payable within a year.
20. **Interpretation of Current Ratio:** The ideal current ratio is 2: 1. It indicates that current assets double the current liabilities are considered to be satisfactory. Higher value of current ratio indicates more liquid of the firm's ability to pay its current obligation in time. On the other hand, a low value of current ratio means that the firm may find it difficult to pay its current ratio as one which is generally recognized as the patriarch among ratios.

TABLE 1:

	2010-11	2011-12	2012-13	2013-14	2014-15
current assets (Rs. in crores)	26,590.97	36,759.74	38,230.64	39,736.78	27,599.48
current liabilities (Rs. in crores)	19,606.60	42,700.36	43,262.65	35,307.26	23,695.30
current ratio = current assets/ current liabilities	1.35623	0.86088	0.88369	1.12546	1.16477

(2) Quick Ratio (or) Acid Test or Liquid Ratio

Quick Ratio also termed as Acid Test or Liquid Ratio. It is supplementary to the current ratio. The acid test ratio is a more severe and stringent test of a firm's ability to pay its short-term obligations 'as and when they become due. Quick Ratio establishes the relationship between the quick assets and current liabilities. In order to compute this ratio, the below presented formula is used :

Liquid Ratio=Liquid Assets (Current Assets - Stock and Prepaid Expenses)/Current Liabilities

Quick Assets = Current Assets - (Inventories + Prepaid expenses)

The ideal Quick Ratio of 1: 1 is considered to be satisfactory. High Acid Test Ratio is an indication that the firm has relatively better position to meet its current obligation in time. On the other hand, a low value of quick ratio exhibiting that the firm's liquidity position is not good.

TABLE 2:

	2010-11	2011-12	2012-13	2013-14	2014-15
current assets (Rs. in crores)	26,590.97	36,759.74	38,230.64	39,736.78	27,599.48
inventory (Rs. in crores)	16,622.28	19,454.53	16,438.70	18,775.41	12,972.26
quick assets = current assets - total inventory (Rs. in crores)	9,968.69	17,305.21	21,791.94	20,961.37	14,627.22
current liabilities (Rs. in crores)	19,606.60	42,700.36	43,262.65	35,307.26	23,695.30
Quick ratio = Quick assets/ current liabilities	0.508435425	0.405270822	0.503712556	0.593684415	0.617304698

Absolute Liquid Ratio:

Absolute Liquid Ratio is also called Cash Position Ratio (or) Over Due Liability Ratio. This ratio established the relationship between the absolute liquid assets and current liabilities. Absolute Liquid Assets include cash in hand, cash at bank, and marketable securities or temporary investments. The optimum value for this ratio should be one, i.e., 1: 2. It indicates that 50% worth absolute liquid assets are considered adequate to pay the 100% worth current liabilities in time. If the ratio is relatively lower than one, it represents that the company's day-to-day cash management is poor. If the ratio is considerably more than one, the absolute liquid ratio represents enough funds in the form of cash to meet its short-term

obligations in time. The Absolute Liquid Ratio can be calculated by dividing the total of the Absolute Liquid Assets by Total Current Liabilities. Thus,

$$\text{Absolute Liquid Ratio} = \text{Absolute Liquid Assets} / \text{Current Liabilities}$$

Limitations of the study

Ratio analysis is one of the important techniques of determining the performance of financial strength and weakness of a firm. Though ratio analysis is relevant and useful technique for the business concern, the analysis is based on the information available in the financial statements. There are some situations, where ratios are misused; it may lead the management to wrong direction. The ratio analysis suffers from the following limitations:

- Ratio analysis is used on the basis of financial statements. Number of limitations of financial statements may affect the accuracy or quality of ratio analysis.
- Ratio analysis heavily depends on quantitative facts and figures and it ignores qualitative data. Therefore this may limit accuracy.
- Ratio analysis is a poor measure of a firm's performance due to lack of adequate standards laid for ideal ratios.
- It is not a substitute for analysis of financial statements. It is merely used as a tool for measuring the performance of business activities.
- Ratio analysis clearly has some latitude for window dressing.
- It makes comparison of ratios between companies which is questionable due to differences in methods of accounting operation and financing.
- Ratio analysis does not consider the change in price level, as such, these ratio will not help in drawing meaningful inferences.

5. CONCLUSION

In a major drive to enhance the petroleum and hydrocarbon sector, Government of India has introduced initiatives like the Hydrocarbon Exploration Licensing Policy (HELP), Marketing and Pricing freedom for new gas production, grant of extension to the Production Sharing Contracts and assigning the Ratna offshore field award to Oil and Natural Gas Corporation (ONGC) for development.

The Government of India plans to incentivize gas production from deep-water, ultra deep-water and high pressure-high temperature areas which are presently not exploited on account of higher cost and risk, and also to augment the investment in nuclear power generation in the next 15 to 20 years.

The Government of India is in the process of identifying at least 50 potential blocks of 100 sq. km and above to be given to companies for bringing private investment in the mineral exploration sector. The Ministry of Petroleum and Natural Gas has put up for comments a draft policy, to opt for revenue-sharing model while auctioning future oil and gas blocks for exploration to private companies, compared to production-sharing mode earlier, in order to make the process more transparent and market-oriented.

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