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Cash vs. net working capital as strategic tools for the long-term relation between bank credits and liquidity: Inequalities in Turkey

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Abstract

Cash and net working capital are among corporate liquidity indicators which are generally compared with the short-term bank credits. The study reveals both the short and the long-term bank credits and their reflections on the cash, working capital and the short-term liabilities of the businesses in the long-run. The bank credits as a financing resource of the real sector (nonfinancial) businesses in Turkey with their effects on cash and net working capital are assessed in order to make comparisons on the total data of the businesses selected from all of the sectors for the case of Turkey in the long-run (1996-2014) in the study. The study endorses the strategic relation between bank credit usage and liquidity levels of the businesses so as to improve timely accessibility and creditability. In the findings, we confirm that cash-cash equivalents and net working capital have impacts on the level of bank credits in the long-term. Finally, the study endorses the strategic relation of bank credit and liquidity by inequalities.

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Keywords: Strategic business finance, cash, net working capital, bank credits, inequalities.

1. Introduction

Corporate working capital is always being among the most considered variables of liquidity. The literature on corporate liquidity analyses working capital (Beaver, 1966) and net liquid assets ever since Altman (1968). Working capital (Altman and Narayan, 1997) or NWC as the difference of current assets and short-term liabilities, sufficient

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liquidity (Chen et al., 2011), and liquidity ratios are among credit score determiners of credit worthiness for the firms of any scale (Abdou and Pointon, 2011). In addition, measuring only the cash may not be sufficient in order to comprehend future paying circumstances (Al-Attar and Hussain, 2004). Nevertheless, net working capital and short term liabilities as in net working capital to total assets ratio (NWC / TA) are among the liquidity indicators which are valid in all industries (Drever and Hutchinson, 2007). Higher short term liabilities result in unstable liquidity (Min and Lee, 2008). Liquidity complications may force businesses to seek bank credit. As the scale of the business is smaller, however, the firms are very sensitive to credit fluctuations and therefore they appear to be bank dependent (Gorton and He, 2008). Banks may even provide credits for risky firms for which liquidity problems are assessed to be temporary (Behr and Güttler, 2007).

Liquidity and its strategic aspects are subject to be utilized as financial criteria. In this context, cash and cash equivalents with net working capital of any business may have effects on corporate bank credit usage in time.

Since cash and net working capital are cited among the most famous liquidity indicators and consist of the assets which are naturally financed by the short-term liabilities and bank credits, the study reveals both the short and the long-term bank credits and their reflections on the cash, working capital and the short-term liabilities of the businesses in the long-run. Therefore in the study, the bank credits as a financing resource of the real sector (nonfinancial) businesses in Turkey and their effects on cash and net working capital are assessed in order to make comparisons on the total data of the businesses selected from all of the sectors for the case of Turkey in the long-run (1996-2014).

The study tries to disclose the level of bank credit used by the businesses through cash and net working capital as well as the comparisons of these liquidity indicators in the long-run upon inequalities. In the findings, we try to confirm that cash-cash equivalents and net working capital have impacts on the level of bank credits used by the businesses in the long-term. Thus, banks may consider the level of cash and net working capital as signs of liquidity for an affirmative and potential creditability in the future. Furthermore, the businesses may also ponder cash holdings and net working capital performance as signs of liquidity requirements to determine potential bank credit need for which they would possibly seek in the future. In the conclusion, the study endorses the strategic relation between bank credit usage and liquidity levels of the businesses through inequalities so as to improve monitoring tools, timely accessibility and creditability. We believe that strategical perspective in corporate finance is to revisit the significance of cash and net working capital in order to determine bank credit potential of the businesses of all scale. Banks, on the other hand, are to enhance detailed valuation for cash holdings and net working capital in their assessment procedures of corporate creditworthiness. However, there is not any direct and technical criterion for this type of evaluation in the related literature.

2. Methodology

The CBRT (the Central Bank of the Republic of Turkey) real sector data consisting of a selection of various business types operating in Turkey are the raw data of the study. We analyzed the series of past three year financial table aggregate totals and aggregate ratios of the businesses for 19 years (1996–2014). We consider randomly selected research data which consists of the values of 51 observations from a total of 152,348 firms and from an average of 8,018 firms for each year in the evaluated time period.

After the considerations, the study discusses the findings of the data set in contemporary data processor software and the calculations of the authors with the related literature and alleges its suggestions on the rankings and differences among the inequalities of the appraised variables with their most repeated rankings, minimums, maximums, and averages in the long-run.

The ratios and financial terms used in the study as the nomenclature are given below.