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The determinants of working capital behaviour: evidence from emerging markets

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Abstract

This study examines the impact of firm-specific and macroeconomic factors on the working capital management of firms listed in the Middle East and North Africa (MENA) region. This research is based on a panel data analysis of 687 non-financial firms listed on eleven MENA stock markets, carried out using the Generalized Method of Moments (GMM) approach. Our results reveal that profitable firms with high levels of operating cash flows adopt a conservative working capital management. Young firms with rapid growth rates, highly leveraged firms, and firms with large investments in fixed assets have higher liquidity needs, which explains their tendency to pursue aggressive working capital strategies. Similarly, large firms exercise their bargaining power over their clients and suppliers to implement an aggressive approach of working capital management. Finally, firms do not have the luxury to decide how working capital should be managed when they are subject to outside macroeconomic forces that affect their stakeholders as well. Our findings can help managers identify the factors that shape their working capital management. Firms in the MENA region maintain excess reserves of cash, which causes under-investment and inefficient allocation of resources in the economy. Improving working capital management practices can allow firms to regain operational efficiency, enhance financial performance, and support economic growth. To the best of our knowledge, this is the first study to investigate this topic in MENA emerging markets.

Keywords: Working capital management; Cash Conversion Cycle; Emerging Markets; Generalized Method of Moments.