Effects of Working Capital Management on Profitability - Empirical Evidence from Euronext Listed Retail Firms

Lina Weng[1], Dr. Amir Moradi[2]
HAN University of Applied Sciences, the Netherlands

Abstract

This paper aims to empirically investigate the effects of various components of net working capital on the profitability of European firms in the retail industry. A balanced panel sample of 19 retail companies listed on Euronext was selected over a period of six years, from 2016 to 2021 to assess the relationship. Results indicate that profitability and inventory turnover in days have a significant positive relationship, while the average collection period has a significant negative relationship. Therefore, if these retail enterprises effectively manage the cash conversion cycle and maintain optimal levels of accounts receivables and inventories, their profitability will increase. This paper provides two recommendations for practitioners. First, the retail companies' management should lower the number of days' account receivable, which increases the actual profit and consequently increase profitability. Second, the company should keep a reasonably large inventory level to lower the risk of product scarcity and to cut expenses when prices are fluctuating, both of which lead to higher profitability.

Keywords: Average collection period; inventory turnover in days; average payment period; cash conversion cycle; current ratio.