



Cost Leadership Through Effective Working Capital Management

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ABSTRACT

Two way efforts from government and enterprise are needed to undertake to get cost leadership in the modern era of cut throat competition. This is a new mechanism which uses working capital management as tool to reduce cost of production and price of the product in the market. This article mainly focuses on developing rather integrating some techniques of firm with the support of government in its implementation. This paper mainly suggested some of the ways through which an enterprise can manage its working capital by joining their hands with government.

Keywords : Working capital, Cost leadership

Introduction

The world becomes global where each organization wants to be competitive to emerge as a best player in the market. This competitiveness would be achieved by putting either of following course of action in practice.

- (1) Differentiation
- (2) Low cost leadership
- (3) Focus

If any company wants to get success in emerging countries like India, China and Brazil which are growing at a tremendous pace, their main focus has to be on cost leadership. It is because of reason that people are more conscious about price. Because of it if company sets lower price for their product, they will get huge demand for it. i.e. Product of China is demanded more in market of India.

Now the question is that how to sale product at a lower price? An organization can solve this problem by reducing their cost of production, as there is direct relation prevailing between price and cost of production. Company can achieve it by reducing requirement of working capital.

What is Working capital?

Working capital refers to that part of capital which is not tied up in fixed asset but is used to meet day to day requirement of business. It is invested in current assets like Cash, Stock, Bills receivable, Debtors etc. This type of capital is use to make payment for purchased of raw material, wages and to meet other expenses till goods sold and money is collected against it. The stock are to be maintained continuously meet demand for product and some money is tied up in the credit sales. Capital used for these purpose is called working capital.

Working capital may be require permanently or variably.

Permanent working capital

It consists of the working capital which is necessary for maintaining stock of raw material and finished goods at normal level and for paying wages and salary regularly. It is minimum amount of current assets which is needed for the smooth running of business.

Variable working capital

It deals with that working capital which is needed to meet the seasonal demand and special needs. This is called variable

working capital because it is amount varies according to the extent of extra demand.

It is clear that the main components of working capital would:

- (1) Closing Stock
- (2) Receivable
- (3) Cash

If we want to cut down requirement of working capital then we are required to deal efficiently with these. To do business with lower working capital, two ways efforts is likely to be put by firm and government.

(A) How government helps in minimizing working capital requirement:

Government helps us to minimize W.C requirement by providing following facilities:

- (1) Location benefits
- (2) Special Economic Zone
- (3) Infrastructure facilities at competitive price

(1) Location benefit

The government is require to give some incentives to a company which located either nearby availability of raw material or market for finished goods which leads to smooth flow of Raw material/ finished goods from its supplier. It resulted into less stock of raw material / finished goods to be held by company and it ultimately reduce the requirement of working capital. Availability of Raw material or Market for finished goods near to manufacturing units reduce transportation cost that result in reduction in requirement of raw material. i.e. Jindal Steel Ltd. is located in orissa because of availability of Iron-Ore. Government has given some tax incentive to it for selecting this location.

(2) Special Economic Zone

Special Economic Zones for identical product and its ancillary product if declared by government, it motivates the various organizational units to establish their plant close to each other. That ensures easy availability of various parts at desired time and at lowest cost which results in to requirement of less working capital and smooth running of a organization.

Ex: Area near to "Sanand" Village is declared as an Automobile Zone by the Government of Gujarat Where Companies Like Ford, Maruti Suzuki, Tata are going established their plants. Because of it so many companies dealing with its ancillary parts are also moved to that region for smooth supply of necessary parts to the organizations of equipment manufacturing (OEMs).

(3) Infrastructure facilities at competitive price

Organization for its smooth running of production is require necessary infrastructure facilities i.e. Transportation, Electricity etc. If government providing these facilities at lower cost then it also put pressure of cost control on private corporate to match their price with competitor to sustain its market share. It helps to the organizations which are the consumer of these services in lower down their requirement of day to day expenses to be spent on availing infrastructure facilities.

The above discussion has been best understood by government of China, we all are experiencing the result of it. Companies from China are providing goods at so lower cost that it's beyond imagination from their competitors form rest of the world to match their prices with the rival from china. These Companies are getting this advantage because of support of government on various facilities.

(B) How firms can minimize working capital requirement:

Organization without support from government can also control their working capital by implementing following techniques:

- (1) Supply Chain Management
- (2) Just In Time
- (3) Lean Manufacturing
- (4) Total Production Maintenance

(1) Supply Chain Management (SCM)

SCM Mainly focuses on maintaining best coordination with supplier of raw material used by an organization. In the era of innovation we can also use sophisticated technology for

implementing these techniques. It has been best understood by "Walmart" a biggest retail store in the world. It helps in smooth flow of material from supplier as and when we need it due to that organization can work with even ZERO stock of inventory. An inventory forming a larger part of total working capital, minimize the requirement of it ultimately reduce the working capital.

(2) Just In Time (JIT)

It invented by Japan, main focus of JIT is also on reducing inventory holding. As per this technique organization is require to place an order for desire material when the actual requirement arise. Most of the MNCs are using these for the control of stock of inventory held as stock. Here also best coordination with supplier helps to get material on time.

(3) Lean Manufacturing

Lean Manufacturing concentrates on reducing wastage of time and material at each stage of production when it carried out through various stages. It also eliminates the unnecessary steps in production process. Reduction in wastage of material helps in save cost of raw material and reduction in time minimize the cost of labour. Both the action reduce requirement of working capital.

(4) Total Production Maintenance (TPM)

TPM has been founded by Toyota Motors Ltd. It mainly deals with reduction of cost at every stage of assembly line. This technique mainly used by manufacturing organization which dealing with assembling various parts of product. It also focus on reduction of wastage time and material as like lean manufacturing but it mostly used in mechanical products where assembling is required.

Conclusion

Management of working capital efficiently and effectively helps an organization to work with minimum capital. Which results in fewer blockages of it and cost of capital i.e. interest also reduce which in turn decrease the total cost of production. An enterprise can offer their product at lower price than its rivals by achieving cost leadership with help implementing above discussed techniques.

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