Liquidity Assessment of Pakistan State Oil and Shell Pakistan-A Comparative Study

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Abstract
The main objective of this study is to comparatively analyze the liquidity position of Pakistan State Oil and Shell Pakistan by using liquidity ratio analysis and techniques. The significance of this study shows that it provide clear liquidity picture of both companies as well as identifies role of liquidity in oil market. The secondary data was used in this study to analyze liquidity for the year 2013 to 2017, data has been collected in the form of annual report which was taken from company's official websites. Both companies are playing an important role in oil industry of Pakistan. Findings of both companies indicates that Pakistan State Oil shows excellences in the liquidity management then Shell Pakistan. The liquidity ratios show that Pakistan State Oil is better than Shell Pakistan for the year 2013 to 2017. Shell Pakistan should bring improvements in liquidity. As liquidity plays key role in the business both companies must put liquid resources like T-bills and marketable securities to increase their liquidity position in the market, similarly both Pakistan State Oil and Shell Pakistan must try to improve net profit as well.
Keywords: Liquidity, Pakistan State Oil, Shell Pakistan

1. Introduction

1.1 Background

Oil is a major component of global economy. It's useful in all industry whether its food, technology or manufacturing industry, all industries must need it. While there could be alternative way to produces electricity but there is no more substitute of oil in the transportation.
Liquidity measures that a company has sufficient cash to meet its short term obligations, some other assets also comes under liquidity which can be easily converted into cash.
Liquidity management is basically company's ability to fulfil financial commitments over their cash flows, funding activities and capital management. (Jim Negus)
Liquidity ratios identifies liquidity conditions of firm. Liquidity ratios further classifies Current ratio, Quick ratio, and Cash ratio.
In India liquidity management consider as a key component and has significant impact on profitability of oil companies. Additional and insufficient liquidity put companies in numerous problems. In fact, India is 4th important user of oil in the world. (Bhuniaand Bandyopadhay Aug 10, 2015).

In Pakistan liquidity position has also impact on profitability of oil and gas companies. Where current, quick and cash ratio management is most important for a company to management of liquidity. (Saleem and Raheman, 7, July 2011)

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Pakistan State Oil is the largest petroleum distributor and marketer in oil industry of Pakistan. It works within 3689 petroleum filling stations. PSO is the market leader of oil industry in Pakistan with the overall market share of 55% where black product share 69% and white oil 46%.

1.2 Purpose of the Study

As early mentioned liquidity plays an important role in success and failure of business. So this study comparatively analyses the liquidity of PSO and Shell, both are successful business in oil industry of Pakistan. The purpose is to evaluate the liquidity position of both. However, current assets and current liabilities are key role in liquidity management so here it is identified how efficiently both companies are managing current assets to fulfill their short term obligations.

1.3 Research Questions

- What is the liquidity of PSO and Shell?
- Which is better in current ratio management?
- How efficiently both companies manage quick ratio?
- Which one is strongly managing cash ratio?

1.4 Significances of the Study

According to Smith (1980),most of the corporate finance have focused on their long term assets and liabilities, however short term assets and liabilities play meaningful role in particular business, because efficient management of short term assets and liabilities pushes firm forward to achieve its goals.
This study analyze the liquidity position of PSO and Shell Pakistan.

2 Literature Review

2.1 Liquidity Management

According to Njure(2012) Liquidity refers the ability of firm to payout its short term financial obligations as well convert current assets into cash without bearing of loss. Unless a firm will not grow if it does not have a good liquidity position. Some important ratios make significance impact on liquidity position included Current ratio It find through Current assets / Current liabilities, Quick ratio it finds through cash+ account receivables / Current liabilities, and cash ratio cash and cash equivalent + available for sale securities / Current liabilities.
According to Canina et all(2008), Liquidity management is important to attract investors because when investors are going to invest in short time period they always evaluate the liquidity of firm. That’s why liquidity evaluation is most important for both creditors and investors either firm is defaulter or not. Financial statements will help both creditors and investors to evaluate liquidity position of firm. They always look into key liquidity ratios like current, quick, and cash management ratio. A firm could be less risky if its liquidity ratios are same/greater than industry liquidity average.

2.2 Liquidity Management in Financial Institutions

According to Rais and Majid(2003), Financial Institutions broadly focus on liquidity management. Liquidity risk is major for both Islamic and commercial banks because it covers day to day expenses less liquidity increase liquidity risk and liquidity risk leads to bank defaulter or bankruptcy, those who did not manage their liquidity position they became failure in the race of business. That's why liquidity management is one of the key component of the financial institution.

2.3 Current Assets Management

According to (Deloof and Jegers 1996) the core objective of a firm is too maximize profit. But, managing liquidity is also important. So the problem is if a firm increase liquidity position it may get less profit. It may not survive in future same as if a firm don't manage its liquid position the result would be fail in the business. They must manage the optimal level of liquidity which put positive impacts on both liquidity and profitability. Because optimal level of liquidity help to maximize the value of business.

According to Afza and Nazir(2005) assets are categorized into current assets and non-current assets. Where current asset plays vital role in operating activities. A firm may acquire non-current assets on rent but it may not do the same things with current assets. A firm would reduce liquidity risks if it highly invest on current assets. It's not enough highly invest on current assets, the efficient management of current asset is also important. Because the highly invest into current assets may reduce liquidity risks it may also reduce the profitability so the result is firm should invest optimal level into current assets where it will not affect the profitability.

2.4 Cash Management

According to Owolabi and Obida(2012) cash management is important factor of the liquidity management. It defines profitability of a firm, mostly businesses face difficulties to manage minimum cash level management. The minimum cash level is necessary because it manages day to day operating expenses. Large amount of cash in hand shows inefficiency of business firm must have enough cash to fulfill its day to day activities.

According to Shah and Sana(2006), Working capital is an important component to identify the liquidity position of business.

Working capital = current assets – current liabilities. Negative working capital shows that firm have high current liabilities than current assets, firm must maintain positive working capital current assets should be greater than current liabilities otherwise firm will not survive in future. A firm must have enough liquid assets to fulfill its day to day activities like it should have enough cash to pay salaries and meet other operating activities.

According to Panigrahi(2013), In past mostly firms were focusing on long term capital budgeting but now in this era most of them from various industries are focusing on management of efficient working capital where positive working capital shows access amount of current assets than current liabilities, on other hand negative working capital indicates that current liabilities are greater than current assets.

3. 1 Research Methodology

This study focus on the quantitative data, it's an explanatory research and the secondary data is used for the purpose of the study. The unit of analysis of research project is to compare two organizations. Liquidity ratios of both companies are calculated form data.

3.2 Data Collection

The secondary data was collected to be used in this study.Source of data collection were websites of both PSO and Shell Pakistan and website of Pakistan stock exchange commission. The annual report of both PSO and Shell are used as a source of data collection. The data of five yearsfrom 2013 to 2017 was collected from financial statements of both companies.

4. Results and Findings

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4.1 Analyzing the data

PSO

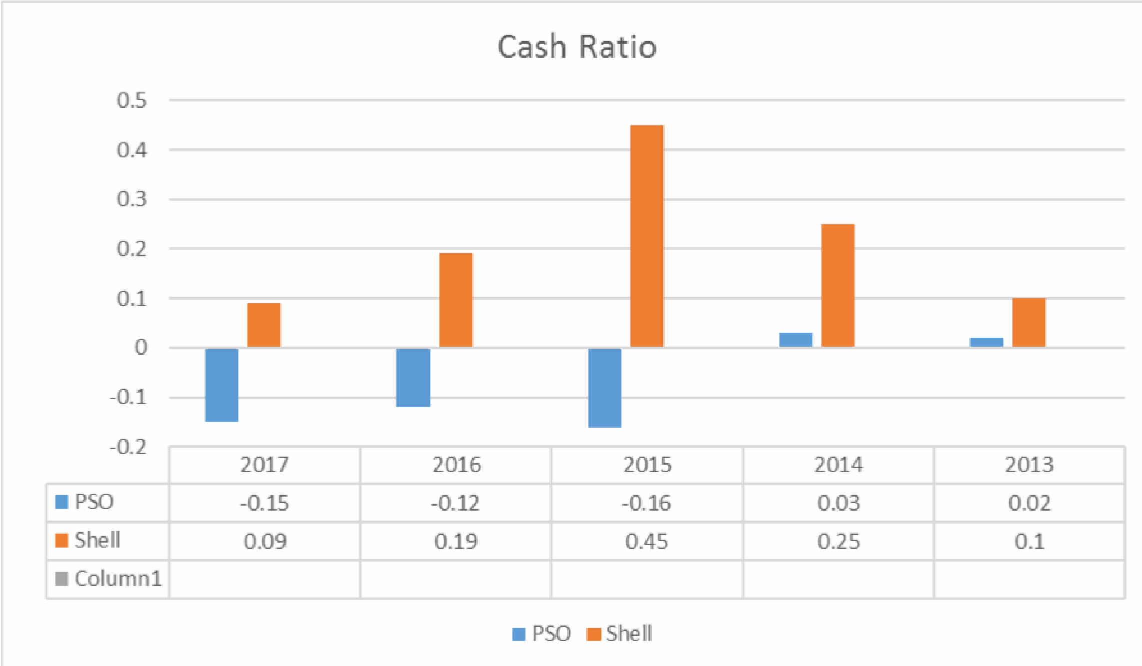
Liquidity Ratio	**2017**	**2016**	**2015**	**2014**	**2013**
Cash ratio	-0.15	-0.12	-0.16	0.03	0.02
Current ratio	1.31	1.12	1.1	1.09	1.03
Quick ratio	1.07	0.91	0.87	0.79	0.54
Mean	**0.743**	**0.637**	**0.603**	**0.637**	**0.530**
S. Deviation	**0.783**	**0.664**	**0.671**	**0.546**	**0.505**

Shell Pakistan

Cash ratio	0.09	0.19	0.45	0.25	0.1
current ratio	0.82	0.87	1.32	1.16	1.11
quick ratio	0.47	0.53	1.09	0.93	0.79
Mean	**0.460**	**0.530**	**0.953**	**0.780**	**0.667**
S. Deviation	**0.365**	**0.340**	**0.451**	**0.473**	**0.516**

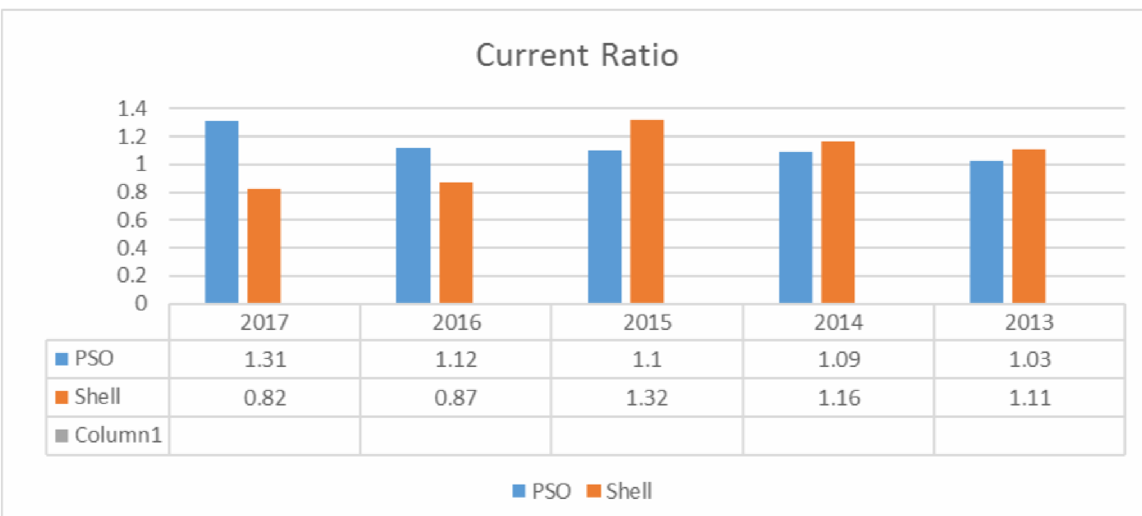
Cash ratio

It shows that firm has enough cash to manage its day to day activities and short term obligations. The cash ratio of Pakistan state oil lower side of ratio from 0.02 in 2013 to -0.15 in 2017. Where the ratio of Shell Pakistan also has decreased from 0.1 in 2013 to 0.09 in 2017 but in terms of compression Shell Pakistan has higher cash ratio then Pakistan state oil it's further elaborated in graph.



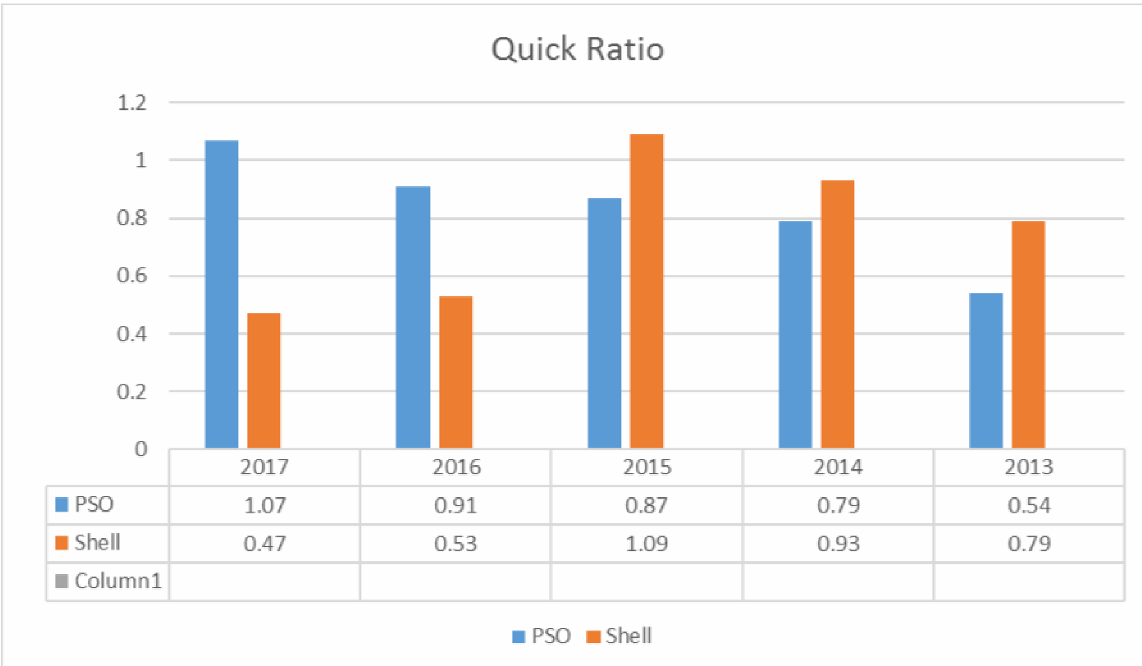
Current ratio

It shows that a business has enough current assets to fulfill its current liabilities. The Current ratio Pakistan state oil indicates higher side of ratio from 1.03 to 1.31 from 2013 to 2017. Where Shell Pakistan has decreased its current ratio from 1.11 to 0.82 from 2013 to 2017. It can be concluded that Pakistan state oil is showing efficiencies its current assets then Shell Pakistan further it's elaborated in graph which is given blow.



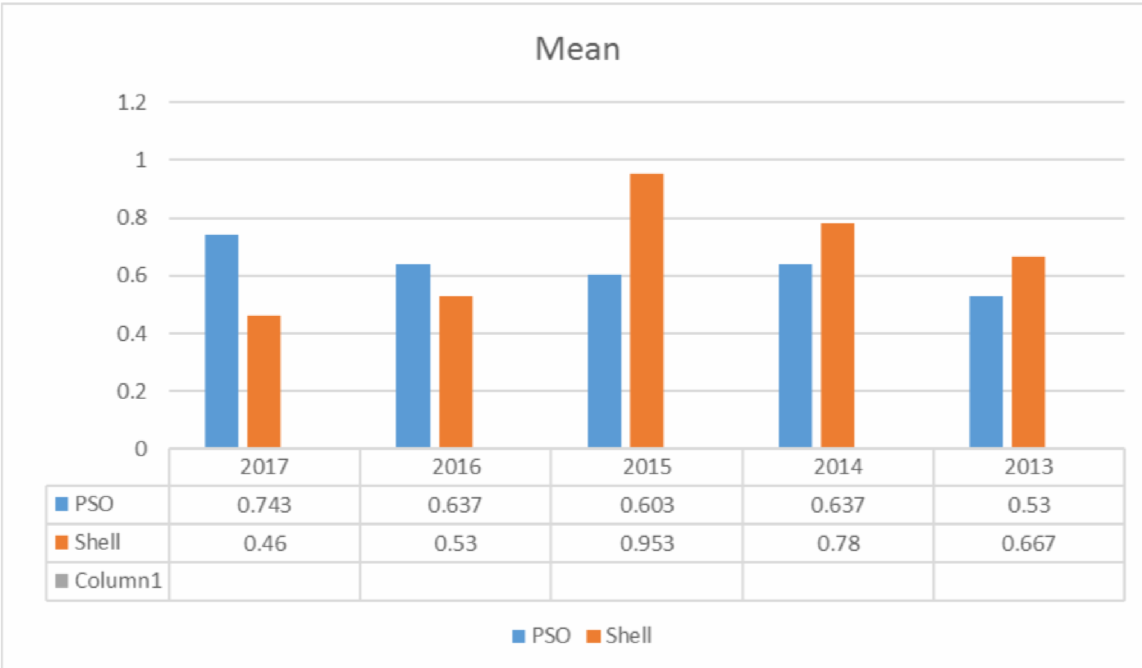
Quick ratio

It's also known as Acid test ratio, it shows business ability to manage quick assets to meet current liabilities. So the quick ratio of Pakistan state oil has increased from 0.54 to 1.07 from 2013 to 2017. Where Shell Pakistan has decreased its quick ratio from 0.79 to 0.47. It can be concluded that PSO has higher quick ratio then Shell Pakistan.



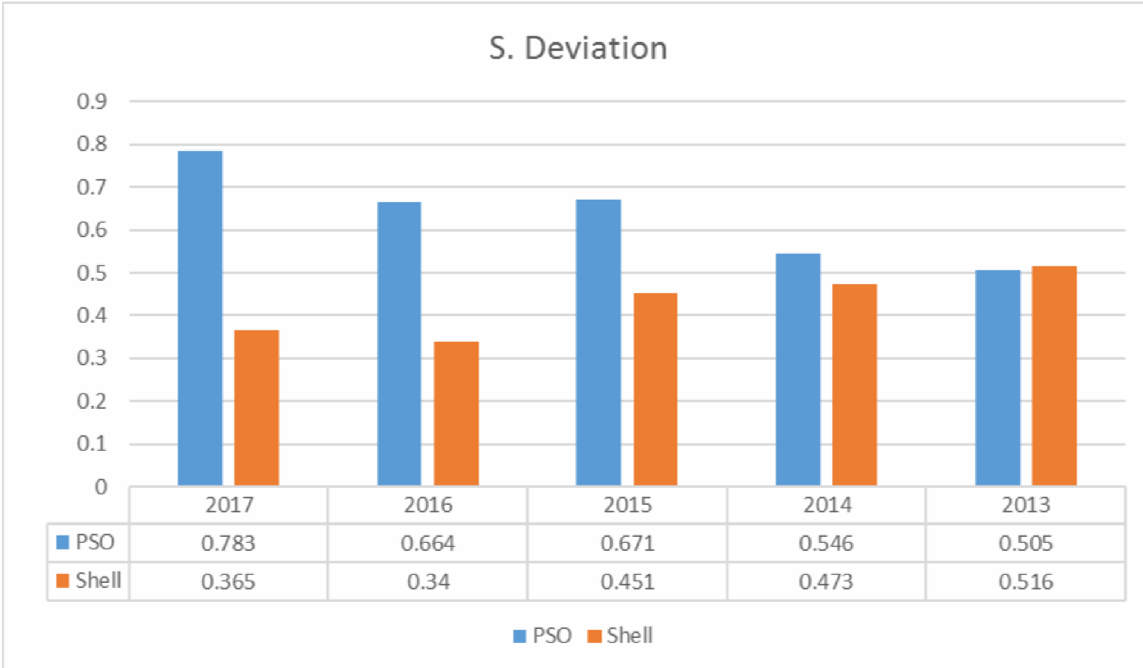
Arithmetic Mean of all Liquidity ratios

It's an average of the numeric values. The average value of each ratio from 2013 to 2017 has found by which this research can be clearly identify the liquidity position of both companies. So in this research PSO average value has increased from 0.530 to 0.743 from 2013 to 2017. Where Shell Pakistan average value has drastically changed over the five year, currently its lower side 0.667 in 2013 to 0.460 in 2017, it can be concluded that PSO indicates higher average then Shell Pakistan the graph is mentioned blow.



Standard Deviation

In finance standard deviation used to measure fundamental risk of a business. In this research Deviation used to calculate risk of both companies so after calculation PSO standard deviation has increased from 0.505 to 0.783 from 2013 to 2017. Where Shell Pakistan has decreased by 0.516 to 0.365 from 2013 to 2017. It can be concluded that PSO has higher risk then Shell Pakistan.



4.2 Answering the research question

RQ1, foremost important question of my research is that what is the liquidity of PSO and Shell Pakistan? This research has identified that Pakistan state oil has higher liquidity then Shell Pakistan

RQ2, which is better in current ratio management?

	2017	2016	2015	2014	2013
PSO					
Current ratio	1.31	1.12	1.1	1.09	1.03
Shell Pakistan					
current ratio	0.82	0.87	1.32	1.16	1.11

Pakistan state oil has greater current ratio 1.031 in 2013 to 1.31 in 2017 during these years PSO has positive change in current ratio it indicates only change of 35% during the period of 2013 to 2017 where Shell Pakistan has lower current ratio from 1.11 to 0.82 from 2013 to 2017. It is negative change during these years only 2015 has highest current ratio 1.32 rest of the year it declined which indicates that Shell Pakistan has -29% during these years so the result is Pakistan state oil is better in current ratio management then Shell Pakistan.

RQ3. How efficiently they manages their quick ratio?

	PSO				
	2017	**2016**	**2015**	**2014**	**2013**
Quick ratio	1.07	0.91	0.87	0.79	0.54
Shell Pakistan					
quick ratio	0.47	0.53	1.09	0.93	0.79

In compression of quick ratio Pakistan state oil has higher side, it has positive cash ratio from 0.54 to 1.07 from 2013 to 2017 it indicates positively change over the time period only change of 53% during the year 2013 to 2017 On other hand Shell Pakistan is in lower side from 0.79 to 0.47 from 2013 to 2017 which goes negative side over the years 2014 and 2015 has highest quick ratio which is 0.93 and 1.09 if we conclude it Shell Pakistan made -32% change during 2013 to 2017 So it can be concluded that Pakistan state oil is efficiently managing its quick ratio then Shell Pakistan.

RQ4. Which one is strongly managing its cash ratio?

	PSO				
	2017	**2016**	**2015**	**2014**	**2013**
Cash ratio	-0.15	-0.12	-0.16	0.03	0.02
Shell Pakistan					
Cash ratio	0.09	0.19	0.45	0.25	0.1

In this case Pakistan state oil has lower side from 0.02 in 2017 to –0.15 in 2017 which shows negative change in the cash ratio management by PSO which is -13% change on other hand Shell Pakistan also decreased its cash ratio cash ratio from 0.1 in 2013 to 0.09 in 2017 but in 2014-15 it had positive cash ratio after these years it again declined. But if we see figures it clearly tells Shell Pakistan is good then PSO. According to research question both are not strongly managing their cash ratio. But in this situation as a researcher we can say Shell Pakistan is little bit better than Pakistan state oil. An average and Deviation has further identified the deep liquidity position of both companies.

	PSO				
	2017	**2016**	**2015**	**2014**	**2013**
Mean	**0.743**	**0.637**	**0.603**	**0.637**	**0.530**
Shell Pakistan					
Mean	**0.460**	**0.530**	**0.953**	**0.780**	**0.667**

So the an average of Pakistan state oil has increased from 0.530 in 2013 to 0.743 in 2017 it indicates only change of 21.3% positively during the year 2013 to 2017 on other hand Shell Pakistan has lower is in an average from 0.667 in 2013 to 0.46 in 2017. In 2014 and 2015 it had higher average 0.780 and 0.953 which was appreciable then PSO but again it went to decline I can be concluded that liquidity position of Pakistan state oil is better than Shell Pakistan.

		PSO			
	2017	2016	2015	2014	2013
S. Deviation	**0.783**	**0.664**	**0.671**	**0.546**	**0.505**
	Shell Pakistan				
S. Deviation	**0.365**	**0.340**	**0.451**	**0.473**	**0.516**

If we talk about Standard Deviation Pakistan state oil has also increased by 0.505 to 0.783 from 2013 to 2017 it indicates 27.8% change in the risk level of PSO which is not good for Pakistan state oil where Shell Pakistan has decreased by 0.516 in 2013 to 0.365 in 2017 it indicates -15.1% change negatively during these years it means Shell Pakistan has less risk then PSO in the management of liquidity. But if we see result in 2017 Deviation has again increased which is not good Shell Pakistan should control it otherwise it would be dangerous for them. It can be concluded that Pakistan state oil has higher risk in management of liquidity then Shell Pakistan. It simply shows that's higher the risk higher the profit.

RQ5, Will make recommendation for improvement of liquidity?

Shell Pakistan is lower side in liquidity management then Pakistan state oil. Shell Pakistan should improve liquidity otherwise it would be destructive for the business and might face many difficulties in future due to lack of liquidity.

5. Conclusion, Discussion, Limitation and Recommendations

5.1 Conclusion:

The main purpose this study was to comparatively analyze the liquidity of PSO and Shell Pakistan on the basis of five years data from 2013 to 2017. It is concluded that the liquidity management of Pakistan State Oil is better than Shell Pakistan in terms of all liquidity ratio's such as Current ratio, Quick ratio except cash ratio Shell Pakistan is only performing better in cash ratio management which shows weak position in liquidity management because the average of these ratio clearly elaborate that PSO has strong position in the management of liquidity then Shell Pakistan. But Pakistan State Oil has high Deviation it means high volatile and more risk than Shell Pakistan. PSO must overcame this for future betterment.

5.2 Discussion:

In this study secondary data was used as well different ratio analysis techniques methods were also utilized. The main purpose of this study was to identify the liquidity position of both petroleum companies with the help of different liquidity ratio's analysis techniques such as cash ratio, current ratio, and quick ratio. Our findings show that Shell Pakistan has higher Cash ratio management then Pakistan State Oil, (Owolabi and Obida, 2012) reported that cash management is important factor in the liquidity management because it's necessary to maintain minimum cash level which covers day to day operating expense. So according this PSO should improve cash ratio and keep maintain minimum level of cash for operations. Further findings show that PSO has higher current ratio management then Shell Pakistan according to (S.M Amir Shah and Aisha Sana, 2006) negative working capital shows that firm has high current liabilities then current assets which is harmful for business. Firm has to manage positive working capital for being a successful in market. So in order to this Shell Pakistan should improve its current ratio management. In last findings show that in quick ratio and overall liquidity management PSO has higher than Shell Pakistan in the prior studies (Kimondo Charles, Njure, 2012) reported that business must have enough liquidity to fulfill short term activities because insufficient liquidity is harmful for business. In Other prior study (Linda Canina, Steve, A, Carvel, 2008) reported that liquidity management is important to attract short term investors because they always evaluate liquidity before making investment. They always looks liquidity ratios current cash and quick ratios. So for finding the result of this research has taken the data of five years from 2013 to 2017. In last the outcomes has been find out by the annual reports of both companies.

5.3 Limitation

The limitations of this study is to that only liquidity ratios are calculated, in fact it doesn't give complete picture regarding business performance because for checking business performance profitability ratios to be calculated.

5.4 Recommendation

Shell Pakistan has more liquidation issues, it must put more liquid assets like attractive securities and T-bills to overcome liquidity challenges. This study further suggests that Pakistan State Oil should improve cash ratio because since 2013 to 2017 cash ratio has negative growth which is not good for PSO and its whole business. Overall liquidity position of PSO is performing well then Shell Pakistan.

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