

"Sustainable Growth vs. Financial Flow: Unlocking the Growth Potential of Indian Textile Companies" investigates the correlation between cash flow and SGR

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Abstract

In this paper, the author delves into whether the Sustainable Growth Rate (SGR) has a similar relationship with the other cash flow items, namely; Cash Flow of operating activities, (CFO), Cash Flow of Investing Activities, (CFI) and Cash Flow of Financing activities (CFF) in the 10 listed companies in the Indian textile industry, in respect to the period between the years 2015 to 2024. With the help of secondary data presented in the financial reports of the company and using the Pearson correlation methodology through the use of SPSS, the paper will measure the effect of the both inner and outer finances on the sustainable growth of a company that supported long-term. The results indicate the low positive relationship between SGR and CFO and the low relationship or negative relationship between CFI and CFF which is insignificant. These findings reveal that the operational efficiency (CFO) contributes very little in the growth and the investment (CFI) and financing (CFF) operations contribute very little to the sustainability. However, a statistically viable and negative correlation ($r = -0.842$, $p = 0.002$) between CFO and CFF can be traced, which implies that a firm is extremely open in its internal cash generation

machinery and the lesser it resorts to outside capital. This is in agreement with the pecking order theory whereby the firm prefers internal over debt or equity funding. Altogether, the researcher concludes that sustainable growth in Indian textile industry has some rather loose connections with short time cash flows and is defined rather by the strength of the operation and financial plan than by anything relating to the accessibility of capital. In order to augment the results of sustainability, it is recommended that one must concentrate on the efficiency of operation and cautious financing only ought to be carried out in the paper

Keywords: Sustainable Growth Rate, Cash Flow from Operating activity, Cash Flow from Investing activity Cash Flow from Financing activity

Introduction:

Indian textile industry, the backbone of the country in terms of economy, creates many employment opportunities and export revenues, and makes up more than 12 percent of the total export and 45 million workers (IBEF, 2023). Nevertheless, Textile firms exist in an industry environment that is highly competitive, capital-intensive, and cyclical at the same time and that long-term growth and financial management without a high level of financial discipline pose a significant challenge. In this respect, it would be important to learn the financial variables that affect the possibility of a firm to sustainably grow.

The Sustainable Growth Rate (SGR) is one such indicator that is the rate at which the firm can grow by use of internal capital without going to the outside capital and making use of additional financial leverage, and constant on the return on equity and the retention ratio (Higgins, 1977). It gives information as to whether a company should be able to increase operations, buy new assets and pay back shareholders with the aid of in house generated funds. But in the process of having sustainable growth one cannot also leave out the necessary aspect of having enough liquidity and good financial management, which can only be evaluated using cash flow analysis.

A combination of cash flows, related to operating activities, investing activities, and financing activities reflects financial strength and the potential to extend the companies. Cash flow operating activity (CFO) assesses the amount of liquidity provided by the most important functions of business which is important in financing major operations and reinvestments (Palepu & Healy, 2008). Cash flow in investment (CFI) shows the trend in which the firm will go in assets acquisition or disposal and this is directly related to expansion and growth in the long term. Cash flow financing activities (CFF) indicates the source of capital raising or settling debts and dividends distribution thereby affecting the leverage of a firm and growth prospects.

Although there has been a separate treatment of cash flow measures and SGR in the present literature, there is need to have some integrated research into determining the interrelation between SGR and all the three cash flows, especially in the textile industry. Considering its working capital-intensive nature, long production cycles, and a strong dependence on internal

and external financing in this business, the idea of using this industry as a leveraging opportunity is doomed to fail, a holistic examination of these variables is essential.

Literature Review

The sustenance growth is a plank in the financial and strategic planning since the numerous centuries that have gone by. Sustainable Growth Rate (SGR) is the programming in which Higgins (1977) initially modeled it in order to understand how rapidly a firm is expected to grow in terms of its sales, assets and profitability without causing any alteration of the structure of capital trading. The significant variables of SGR comprise two internal variables, namely the earnings retention ratio and the return on equity (ROE). Over the years, this notion has been altered by the researchers to consider the so called internal financial resources, that is the cash flow and the ability with which it renders a firm to grow without risking its financial position or Über-Leveraging.

The Sustainable and Its Determinants

The one report that commands high respect is the SGR that happens to be the internal capacity of the company to expand. The work by Van Horne and Wachowicz (2005) may be used to identify the fact whether the company is developing faster or slower in regards to its financing potential. The tendency is that companies that exceed the sustainable growth level tend to undergo the stresses in terms of their financial position and also to a large degree depend on the external capital. Overburdening the growth capacity on the other hand can lead to the loss of market, and non-efficient use of capital (Higgins, 1981). The utility of the SGR as a forecasting tool has also been understored by research scientists such as Salmi and Martikainen (1994) as far as the financial health diagnostics are concerned. In the recent past, Prasad and Reddy (2020) clarified that standard SGR is a determinant of internal financial dynamics, risk exposure, as well as an ability that a firm is endowed with to manage the operational resources.

Cash Flow as Financial Performance Measurement.

it could be possible that cash flow analysis could allow a multidimensional explanation of liquidity and financial flexibility of a firm particularly when they are categorized into operating, investing and financing categories as in AS 3 or IAS 7. The cash flow operations (CFO) is at times regarded as the most vital of the three since its basic operations lead to flow of actual cash. Firms with strong CFO tend to continue with operations and re-investment (White, Sondhi, & Fried, 2003). Cash flow investing (CFI) indicates the nature of investing capital expenditures and nature of investment of the business. Negative CFI is also positively embraced as a situation in which active reinvestment in the growth assets is experienced (Gitman & Zutter, 2012). Financing cash flow (CFF) on the other hand indicates how a company issues and retires debts and equity in line with its capital structure. As well as such flows are the dividend distribution policy and stock acquisitions that influence the retained earnings and consequently SGR.

Cash Flow and Sustainable Growth Relationship

Several empirical researches have been done on the correlation between the cash flow and a sustainable growth; this is however dependent on location and industry. In a statement of fact, Myers and Majluf (1984) asserted the applicability of operating cash flow financing (i.e., internal financing) in the avoidance of the asymmetric information cost in a syndicated finance. This theory of the pecking order is founded on the fact that the companies are interested in stimulating the internal cash flow to support the expansion and growth and these concepts are linked to the SGR principles to the full extent. Sharma and Kaur (2020) in a study on Indian manufacturing firms develop a positive and close correlation between CFO and sustainable growth and hypothetically state that liquidity of operation will reduce the need of external finance which will escalate financial health of the firm. The applicability of this was also observed in the other study of Velnampy and Pratheepkanth (2012) which examined the Sri Lankan firms and concluded that the greater the operating and financing cash flow of the firm, the more likely to maintain stable SGR.

Quite on the contrary, there are those researchers who found exceptions in industries. Kaur and Singh (2015) discovered that the capital intensive industries like textile require high investment levels through the CFI at a level that is not likely to sustain companies with a high level of ineffective CFO as well as an ineffective capital structure. This helps us note why all the three dimensions of cash flow ought to be analyzed holistically when measuring financial sustainability.

Studies in the Indian Textile Sector

Despite the fact that textile industry constitutes a significant component of the economy, hardly have piles of literature discussed the necessarily of interdependence between SGR and segmented cash flows. Bhattacharyya and Saxena (2019) analyzed the trends in cash flows in Indian textile companies and found out that the working capital is highly volatile thus leading to fluctuating operating cash flow which portrays a negative effect on the long term growth. They emphasized a seasonal and credit-dependent nature of the textile industry and suggested that financial viability of textile industry might be hyper-vulnerable to the liquidity management of any firm. More than that, it is possible to note that Jain and Sharma (2021) discussed the internal finance and its impact on the growth performance of the mid-sized textile companies. They arrived at the conclusion that CFO was significant as an indicator of the growth potential and that irregular or negative CFI (due to disinvestments) had often been shown to lead to the short-run gains of liquidity but the ultimate disadvantage in terms of competition.

Literature Gap

Even though theoretical impact of internal financing and sustainable growth would not be repelled or ambiguous, the bodies of literature pertaining to the joint effects of cash flow of the operating, investing, and financing activities on SGR are identified to be lacking particularly in the Indian textile industry. Earlier works seem to focus on cash flows in isolation or even consider CFO when all the three flows are very much interdependent in strategy. In addition to this, the other studies on the same as far as how the textiles are concerned in specific fields are

still minimal, a fact which further corroborates the need of such thorough textile concerned research which is not only empirical but all comprehensive in its reasoning.

Research Objective: The main objective of this research is to analyse the relationship between cash flow and SGR of selected textile companies.

Research Design

The correlation research design is used in this research since, apart from using one variable as a dependent variable; other variables are independent predictors of the dependent variable. It is one of the 10 listed Indian textile companies and the secondary data has been compiled between 2015- 2024 using the annual reports and the financial databases. The descriptive statistics, Pearson correlation are the grounds of using SPSS in data analysis. Diagnostic tests also provide validation of measure accuracy of a model. The research question would aim at establishing the long term sustainable growth of textile companies to internal and external cash flows whereby there is considerable correlation.

Table.1 Correlations analysis between Sustainable Growth Rate and Cash Flow from Operation (CFO), Cash Flow From Investing Activity (CFI), Cash Flow From Financing Activity (CFF)

		SGR	CFO	CFI	CFF
SGR	Pearson Correlation	1	.154	.044	-.192
	Sig. (2-tailed)		.671	.904	.594
	N	10	10	10	10
CFO	Pearson Correlation	.154	1	-.585	-.842**
	Sig. (2-tailed)	.671		.075	.002
	N	10	10	10	10
CFI	Pearson Correlation	.044	-.585	1	.085
	Sig. (2-tailed)	.904	.075		.816
	N	10	10	10	10
CFF	Pearson Correlation	-.192	-.842**	.085	1
	Sig. (2-tailed)	.594	.002	.816	
	N	10	10	10	10

** . Correlation is significant at the 0.01 level (2-tailed).

Analysis of the correlation results presented in Table 1, along with suggestions and future implications:

Correlation Analysis between SGR and Cash Flow Components

SGR and CFO: Pearson correlation between SGR and the cash flow of operations is literarily not significant, but it is positive $r = 0.154$ and $p = 0.671$. This implies that there is a weak positive relationship which means that when cash flows used in operation increase there are likely chances of sustainable growth but the effect is not pronounced to arrive at an inference.

SGR and CFI: The correlation with the cash flow of the investing is a bit insignificant ($r = 0.044$, $p = 0.904$). It could be because outflow of investment does not come along with pay-offs and machines etc. used in the textile industry have such prolonged gestation period that it is not a profitable growth.

- **SGR and CFF:** low negative relationship ($r = -0.192$, $p = 0.594$) is true and it is perhaps possible that the increase of use of the financing activities (debt or equity) may to some extent deteriorate the sustainable growth but this was not significant. The reason might be due to the burden of money or expectations of dividends.

CFO and CFF: the correlation between operating and financing cash flows is extremely negative and, at the same time, also significant (-0.842 , $p = 0.002$). It implies that the firms that generate more cash within internally (CFO) would employ less external funding (CFF) that is in line with the pecking order theory (Myers & Majluf, 1984). It would mean that the healthy companies will use money received inside the company rather than issue additional funds.

Suggestions:

- **Strengthenify CFO:** Companies should also focus on augmenting productivity and working capital management to establish more operating cash flows that are partially positive in the long term development.
- **Balanced Investment Strategy:** The investment cash flow will show poor correlation hence the companies will be expected to take into consideration the performance of the capital investment where the long range investment will be utilized to promote the growth in the future.
- **Prudent Financing:** In this case there is no statistical significance but the value of CFF is negative which implies that the company should not over finance except where it is necessary since it will either compromise shareholders right or increase debt which is may not be able to afford.

Conclusion:

This research paper discuss here was conducted to analyze interdependency of Sustainable Growth Rate (SGR) and different types of cash flows, i.e., Cash Flow under Operating Activities (CFO), Cash Flow under Investing Activities (CFI) and Cash Flow under Financing Activities

(CFF) in respect of the top 10 listed textile industry companies in India over 10-year span (2015-2024). This was to determine whether internal and external financial flows can make much a difference to see the firm grow to be sustainable as it matures.

The Pearson correlation tests have indicated the following significant results:

1. The relationship between CFO and SGR was of a weak positive nature (0.154) but not significant whole ($p > 0.05$). This weak relationship might have been attributed to differences in operational efficiencies of companies, the seasonality nature of the business, and intensive credit sales facility made by textile industries. These affect the direct impact of the operational cash flows on sustainable growth disregarding the fact that theoretically, well CFO ought to affect the internal funding capacity and growth positively.
2. It implies that the correlation coefficient between SGR and CFI is $r = 0.044$ and $p = 0.904$, and that there was virtually no linear dependence between SGR and CFI. This could be associated with the delayed nature of investment returns which is long term. In the textile sector profits tend to materialise after longer periods of time say in the increase of capital plant and machinery or the technology hence the prospect is not directly related to either profits or stock or capital and there is no correlation that people perceive between the high short term correlation strategies which SGR is demonstrating means. Moreover, not every investment may become a growth investment, but it may be a defensive or a replacement investment-oriented one.
3. The ratio between SGR and CFF were inversely weak related ($r = -0.192$, $p = 0.594$). And this, like the previous, has little importance except to show that the more the outside sources of funds (either debt finance or equity finance) are resorted to, the more the traverse against the long run development of a company. This can be either due to an increase in financial obligations such as paying of interests, dividend or due to straining the firm by shareholders in the form of pressure thereby affecting the ability of this firm to reinvest profitably in the long run.
4. It is necessary to mention that a negative correlation was significantly negative and demonstrated high significant correlation between CFO and CFF ($r = -0.842$, $p = 0.002$). This provides a negative relationship between an estimate of the strength of internal operation cash flows of companies and the probability of a firm to utilize the external funds. It is consistent with the pecking order theory on capital structure, where the companies are likely to draw their finances internally and they would prefer to this approach than tapping capital in the form of loans or equity.

The low positive values of absolute correlations of SGR and the specific cash flows show that sustainability of development of textile industry is dependent on the intricate correlation of the following factors: internal efficiency, conditions of market, structure of capital and long-term strategies of investments.

The limited relationship between the CFI and SGR also indicates that both timeliness and efficiency of investments are significant and there is no necessary linkage between the short-term financial performance and the strategic returns.

The converse CFO-CFF does not seem to be as weak and clarifies the ability of internal cash generation to constrain financing risk and financing organic growth

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