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Impact of Fixed Charges Payment on Operational Efficiency of an Organization

***Ashbin Mathew, **Dr. M. Sindhuja**

*Research Scholar, Department of Commerce

**Research Supervisor and Internal Examiner, Assistant Professor

PG & Research Department of Commerce,

Saraswathi Narayanan College, Madurai

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Abstract

The operational efficiency aspect for any business is vital and must be considered by management to earn reliable and sustainable financial performance. Operational efficiency is the proficiency of a corporation to curtail the unwelcome and maximize resource capabilities to deliver quality products and services to customers. Indian has experienced significant transformations since the inception of Bombay Securities exchange in terms of growth due to local and foreign direct investment such that it has emerged fourth in sub-Saharan Africa and one of the most active securities markets in the whole of India. Besides the stable profitability the market has brought to the various listed firms, it has also contributed to the stability of the financial market and economic development of India in general. As a result, the study of financial performance determinants, specifically operational efficiency, has provoked academic research, corporations' management, financial market, and regulatory interests. The objective of this study was to examine the relationship between operational efficiency and the financial performance of firms listed at Tamilnadu and Kerala securities exchange. The study also used the other five control variables, which are: Financial leverage, Liquidity, Size of the firms, capital adequacy, and real interest rates, to also test whether they have a relationship with ROA of firms listed at the NSE. This study covered two years from 2018 to 2020. The descriptive research design was used, and secondary data were collected from the World Bank and the annual reports of firms listed at the NSE. Data were then analyzed using a regression analysis model and statistical software, namely: SPSS version 21 and Microsoft Excel 2010.

Introduction

Every money invested in an organization need its return to the investor which can be measured by its efficiency. The return on investment can be immediate or near future. Based on the port policy we selected, the return pattern will be. Operational efficiency can be used as tool to measure the efficiency of operational cost invested in the organization. Operational efficiency measures the efficiency of profit over operating costs. The greater the operational efficiency, the more profitable a firm is. This is because the entity can generate greater income or returns for the same or lower cost than an alternative. In financial markets, operational efficiency occurs when transaction costs and fees are reduced. When a company borrows money to purchase a fixed asset such as land, a building, or piece of machinery,

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the lender will require security in the form of a fixed charge. This protects them from the risk of non-payment, and allows repossession and sale of the item if the borrower enters insolvency and is liquidated. This arrangement is similar to a mortgage on a domestic property, whereby the borrower does not fully own their home until the loan is repaid, and the lender has the right to repossess the property on default. A similar example is when a company enters into an invoice factoring arrangement – the factoring company 'buys' the value of sales invoices, lends money back to the business, but takes a fixed charge on the sales ledger

Fixed and variable Charges/Expenses

Fixed charges are an expense committed by the organization to pay now or near feature. It can be classified in to two categories as Capital expenses and fixed Operational expenses. Capital expenses are one-time expenses which provide the return in near future periods of time whereas the operational expenses whether fixed or variable provide the benefits immediately. Examples Some of the operational expenses and its classification as under License fee fixed, Office rent fixed, Office utility, variable Office expenses, variable Raw materials, variable Salary, fixe Even some of the expenses are categorized as fixed, sometime it will vary based on the nature of agreement operations.

Literature Review

The Organizational Development Theory Organizational development emerged out of human relations studies when psychologists realized that organizational structures and processes influence worker behavior and motivation. The corporate development is a long-range effort to improve an organization's problem solving and renewal process through more effective and collaborative diagnosis and management of organization culture with the assistance of a consultant facilitator and the use of the theory and technology of applied behavior. Organizational development is simply a process of continuous diagnosis, action planning, implementation, and evaluation, to transfer knowledge and skills to organizations to improve the operational efficiency through expanding their capacity for solving problems and managing future change.

Research Problem

Operation efficiency can be viewed as what occurs when the right combination of people, process and technology come together to boost the productivity and worth of any business operation, whereas driving down the cost of routine activities to a preferred level. The final result is that resources previously needed to manage operational tasks can be redirected to organization. Furthermore, given the strict conditions before a firm listing requires the fixed charges payment on organizational efficiency and its impact on fixed charges payment.

Objective of Study

To examine the relationship between operational efficiency of an organization and its impact of fixed charges payment

Impact of Fixed Charges in Operational efficiency

An organization with higher operational efficiency will generate more profit then others. So, an organization tries to minimize the fixed charges to increase its operational efficiency. Fixed charges on an organization may slow down the operational cycle in the business which may reduce the efficiency of operation result in minimize the profit. This can be explained with small illustration.

Table -1

Particulars	**ABC**	**XYZ**
Cash in Hand	100,000	100,000

Fixed Operational expenses for next month	40,000	10,000
Free cash in hand	**60,000**	**90,000**

The above illustration to mean for next one month organization ABC has fixed operational expenses for INR. 40,000 whereas Organization XYZ have INR. 10,000 only. Both the organization have operational turnover of 3 time with its free operational cash flow and the profit ration is 5% to its total operational cash flow, the profit will be as under.

Table -2

Particulars	**ABC**	**XYZ**
Free cash in hand	**60,000**	**90,000**
Turnover Ratio	3times	3times
Total turnover	180,000	270,000
Add: Fixed Operational expenses for next month	40,000	10,000
Total operational expenses	220,000	280,000
Profit @ 5%	**11,000**	**14,000**

From the above table, we can see that higher fixed operational expenses may result lower profit to the company as fixed operational expenses will always have 1 turnover ratio only. The profit difference will be depending on the turnover ratio of the company. If an organization has only 1 as its turnover ratio, there will no difference in efficiency as both fixed and variable charges will result the same ratio.

Commitments

Another important point to consider while committing on fixed operational charges is the future viability of the business line or activities. If the identified business line or activity has better future, we can have considerable fixed commitments to freeze future increase in operational cost. For example, if we have better future to sell the new product in new region, we can set up warehouse and sales center to reduce the operational cost and future increase in the cost.

Table- 3

Particulars	**Region 1**	**Region 2**
Expected sales in unit	50,000	50,000
selling price	525	525
Transport cost per unit to region from factory	10	10
Warehouse and sales office cost for next year	60,000	-
Total transport cost if we have warehouse	4	4
Total Transport Cost	200,000	500,000
Add: Warehouse and Sales office rent	60,000	-
Total Cost	**260,000**	**500,000**

From the above illustration, we can clearly identify that the transport cost reduced from 500,000 to 260,000 due to setting up of warehouse and sales office at region as compared to direct transport from factory to customer. In this case, we cannot say that the variable operational expenses will always provide better efficiency to the organization. So, we must verify its impact on case to case basis.

Conclusion

Fixed charges are always having its fixed in nature and we have clear cut cost for near future, say next 12 months, whereas the variable charges are variable in nature which may increase or decrease in near future. If we identified that the cost of raw material may increase, we can have contract to freeze the price and we can pay fixed margin money for the same. The difference between margin money and the cost increase will may provide good return compared to profit ratio vice versa. They can conclude that fixed charges have major impact on operational efficiency, we cannot always say that the fixed will reduce the operational efficiency and vice versa.

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