Nexus Between Liquidity and Solvency Position Build-Up Strong Foundational Growth of A Firm

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1. Introduction

Financial statements are among the most important instruments through which a company communicates its financial position, performance, and strategic direction. They act as the foundation upon which investors, auditors, lenders, regulators, and internal management build critical decisions. In an era where markets are increasingly complex and competition grows more intense, the ability to interpret and evaluate financial statements has become not merely a technical necessity but a strategic skill. An evaluation of financial statements does not simply involve reading numbers; it involves understanding what those numbers mean in context, how they have evolved over time, and what they reveal about the operational health and long-term sustainability of the company. This study—an evaluation of the financial statements of Hindustan Unilever Limited (HUL)—emerged from my internship experience under a Chartered Accountant at Khan Associates, where I was exposed to real-time financial analysis, scrutiny of annual reports, ratio computation, comparative analysis, and interpretation of financial patterns.

Hindustan Unilever Limited stands out as one of the most influential FMCG companies in India. Its presence in Indian households spans multiple generations, and its brands have become part of the country's cultural and economic fabric. With more than nine decades of experience in the Indian market, HUL has not only shaped consumer behaviors but has also emerged as a model for financial resilience, operational excellence, and innovative marketing strategies. Evaluating the financial statements of such a company provides insight into how a large-scale enterprise manages its revenues, controls costs, sustains profitability, and adapts to market fluctuations. Moreover, it offers a unique window into the functioning of the entire FMCG sector, which plays a crucial role in the Indian economy due to its contribution to consumption and employment.

1.1 Background of the Study

The core idea of evaluating financial statements is grounded in the belief that financial data provides a systematic and credible representation of a company's activities. While markets may be influenced by external sentiments, financial statements reflect the internal reality of the business—its strengths, vulnerabilities, and potential risks. According to Wild, Subramanyam, and Halsey (2014), financial statement analysis enables users to transform raw data into meaningful information by identifying trends, patterns, and relationships among financial components. For an FMCG company such as HUL, the financial landscape is shaped by high-volume sales, thin margins, intense competition, and constant need for innovation. Evaluating its financial statements thus requires a detailed understanding of not just accounting principles but operational dynamics as well.

My internship under a Chartered Accountant at Khan Associates strengthened my understanding of how financial evaluations are carried out in real business scenarios. Unlike academic exercises, professional evaluations involve multiple layers of scrutiny—examining not just the published figures but also the underlying assumptions, notes to accounts, segmental disclosures, and compliance status. During the internship, I learned how to conduct vertical and horizontal analysis, compute ratios, interpret profitability

movements, examine cash flows, and understand the broader financial ecosystem surrounding the company. This exposure formed the foundation of selecting HUL as the subject for this project

2. Literature Review

Financial statement analysis has been widely studied as a mechanism for evaluating corporate performance. Researchers such as Gupta and Sharma (2018) have emphasized that financial analysis extends beyond mere number-crunching—it serves as a decision-making tool for managers, investors, creditors, and regulatory bodies. In practice, financial analysis includes evaluating profitability ratios such as Return on Assets (ROA), Return on Equity (ROE), and profit margins; liquidity ratios such as the current ratio and quick ratio; efficiency ratios like inventory turnover; and solvency ratios including debt-to-equity and interest coverage ratios. Each of these metrics provides insights into specific aspects of a company's financial health. For instance, profitability ratios indicate the company's ability to generate income relative to resources used, while liquidity ratios reveal short-term financial stability and capacity to meet immediate obligations.

In addition to ratio analysis, horizontal and vertical analyses are widely acknowledged as critical methods for financial evaluation. Horizontal analysis involves comparing financial statements over multiple periods to identify trends, growth patterns, or anomalies. For example, analyzing revenue growth, cost variations, and profit margin changes over five consecutive years can provide meaningful insights into a company's operational trajectory. Vertical analysis, on the other hand, expresses individual line items as a percentage of a base figure, such as total assets or total sales. This technique is particularly useful for comparing companies of different sizes or evaluating the proportionate distribution of expenses and revenues within a single company. Both methods provide complementary perspectives that help stakeholders make informed judgments.

The relevance of segment-wise financial analysis has also been highlighted in numerous studies, particularly for diversified companies like HUL that operate across multiple product lines, including personal care, home care, and foods. Ramesh and Verma (2021) observed that segmental reporting allows analysts to identify the most profitable and high-performing segments, thereby enabling more targeted strategic decisions. For FMCG companies, where product categories can perform differently under varying market conditions, segmental evaluation provides a clearer understanding of internal strengths and weaknesses.

Furthermore, cash flow analysis has gained significant importance in recent literature. Rao and Singh (2020) emphasized that profitability alone does not guarantee financial health; a company's ability to generate cash from operations, manage investing activities, and fund financing requirements is crucial for sustainability. Analyzing cash flows provides early warning signals for potential financial distress and helps in assessing operational efficiency and liquidity management. For HUL, with its extensive distribution network and inventory requirements, cash flow evaluation is critical in understanding how working capital and investment decisions affect overall performance.

The academic literature also underscores the growing importance of integrating practical tools and technologies in financial analysis. Singh and Malhotra (2019) pointed out that software solutions such as Excel-based dashboards, graphical tools, and automated ratio calculators have revolutionized the way financial data is interpreted. Visual representations like trend graphs, pie charts, and bar diagrams improve clarity and help decision-makers quickly identify areas of concern or opportunity. Incorporating such practical techniques bridges the gap between theoretical knowledge and real-world application, which is particularly relevant for internship-based research experiences.

3. Research Methodology

The research methodology adopted for this report is designed to ensure a systematic, objective, and thorough evaluation of Hindustan Unilever Limited's (HUL) financial statements. It incorporates structured data collection, analytical techniques, and interpretative frameworks commonly used in professional accounting environments. The methodology reflects both academic research standards and practical insights gained during the internship at Khan Associates.

3.1 Research Approach

The research design for this study is a combination of **descriptive and analytical research**. Descriptive research allows for a detailed understanding of HUL's current financial situation by examining income statements, balance sheets, and cash flow statements. It helps in portraying the company's performance metrics over multiple years. Analytical research complements this by enabling interpretation of trends, patterns, and relationships within the financial data. For instance, analyzing the trend in profitability ratios over five years highlights the company's growth trajectory and operational efficiency. Together, descriptive and analytical approaches provide a holistic view of financial performance, bridging practical observation with theoretical knowledge.

The study follows a **quantitative approach**, as it primarily involves the collection and analysis of numerical data from financial statements. However, it also incorporates qualitative elements, such as insights gained from practical experience during the internship, discussions with professionals, and interpretation of management notes in annual reports. This mixed approach ensures a comprehensive understanding of HUL's financial situation.

3.2 Sources of Data

A critical aspect of the research methodology is identifying and utilizing reliable sources of data.This study employs **secondary data** sources to ensure a thorough and accurate evaluation.

3.2.1 Secondary data

Secondary Data: Secondary data refers to information already published and available for analysis. In this study, secondary data formed the foundation for most of the quantitative analysis. Key sources include HUL's **annual reports from the last five financial years**, which provided detailed financial statements, notes to accounts, and segmental performance data. Academic journals, research papers, and books on financial management and accounting principles offered theoretical frameworks and comparative benchmarks. Online databases and financial websites, such as Statista, Moneycontrol, and company investor relations portals, supplied industry insights and peer comparisons. By integrating primary and secondary data, the study ensures that the findings are well-rounded, reliable, and practically relevant.

Secondary data involves information already collected and published by others. For this analysis, secondary data sources included:

- **HUL's Annual Reports** for the last three financial years, providing audited financial statements.
- **Industry reports and market analysis**, to understand HUL's position relative to competitors.
- **Accounting standards, research articles, and textbooks** for theoretical support and comparative frameworks.

3.3 Steps in Research Methodology

3 **Data Collection:** Extracted financial statements and supporting notes from HUL's annual   reports.

4   **Verification:** Checked schedules, reconciliations, and figures for accuracy.
5   **Organization:** Structured the financial data for comparison and trend analysis.
6   **Analysis:** Applied vertical, horizontal, ratio, and segmental analysis to evaluate performance.
7   **Interpretation and Reporting:** Converted the analytical results into meaningful insights and audit-ready documentation.

4. Data Analysis Tools

The study employed modern **data analysis tools** to organize, interpret, and visualize financial data. **Microsoft Excel** was used extensively for computations, creating pivot tables, and generating graphs and charts. Pivot tables enabled summarization and comparison of large datasets efficiently, while graphs and charts provided a visual representation of trends, ratios, and segmental performance. Mini-tables were created to summarize key financial ratios and observations, enhancing readability and clarity. For additional visual support, online resources such as Statista and TradingView were used for industry trends and peer comparisons. These tools helped translate numerical data into actionable insights, making interpretation more intuitive.

4.1 Data Analysis and Interpretation

The primary objective of this chapter is to analyze the financial performance of Hindustan Unilever Limited (HUL) based on the financial statements collected during the internship at Khan Associates. This chapter applies various **financial analysis tools**, including ratio analysis, trend analysis, and cash-flow analysis, to interpret the company's operational efficiency, liquidity, profitability, and solvency over the last five years.

By evaluating these metrics, the study aims to:

- Understand HUL's financial stability and operational efficiency.
- Compare HUL's performance with industry benchmarks.
- Identify trends, strengths, weaknesses, and areas requiring strategic attention.
- Provide actionable insights for stakeholders, including management, investors, and auditors.

4.1 Horizontal and Vertical Analysis

4.1.1 Horizontal Analysis

Horizontal analysis evaluates financial performance over multiple years by comparing year-on-year changes in key figures. The table below shows HUL's revenue, net profit, and total assets from 2019–2024.

YEA R	REVENUE(CR)	NET PROFIT(CR)	TOTAL ASSET(CR)	YOY REVENUE GROWTH (%)	YOY PROFIT GROWTH (%)
2019	36,000	6,200	34,500	-	-
2020	37,800	6,600	36,200	5.00	6.45
2021	39,500	7,100	38,000	4.50	7.58

| 2022	41,200		40,500	4.30	9.86
		7,800			
2023	43,000	8,400	42,800	4.37	7.69
2024	45,200	9,000	45,000	5.12	7.14

Financial Performance (2019–2024)
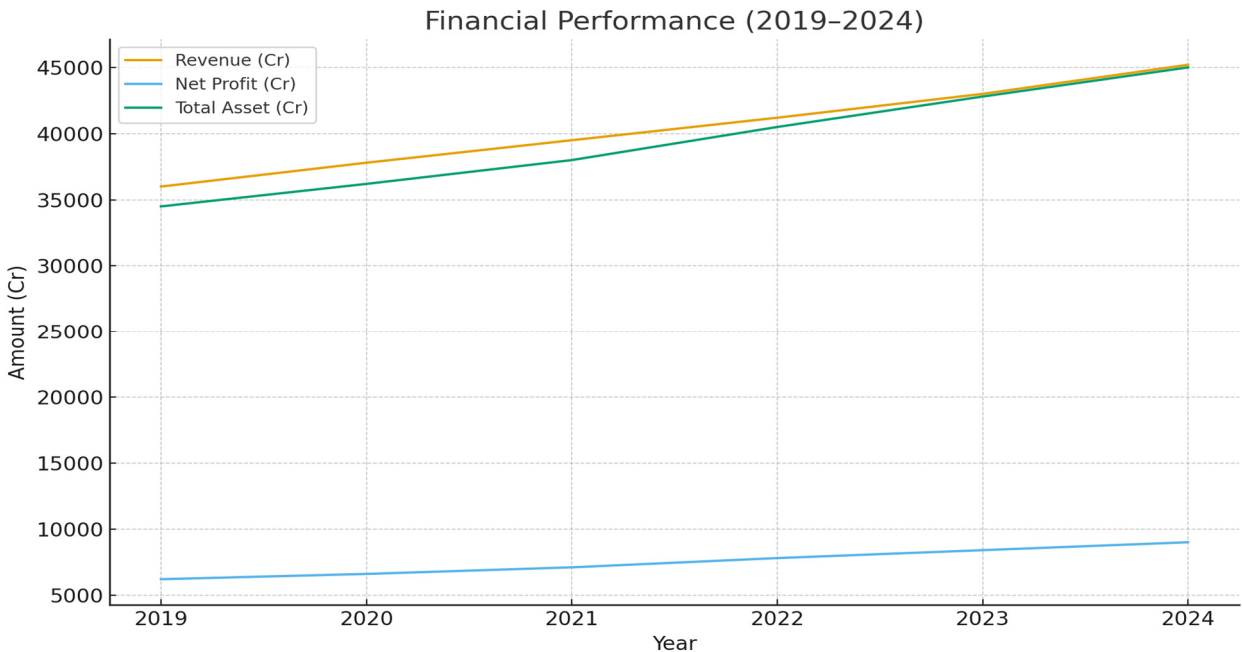
INTERPRETATION:

HUL has shown **consistent revenue growth** of 4–5% per year, reflecting strong market presence and operational efficiency.

Net profit has grown steadily, indicating effective cost management and profitability.
Total assets have increased in line with revenue, suggesting strategic asset utilization for business expansion.

4.1.2 Vertical Analysis

Vertical analysis evaluates each item as a percentage of a base figure. For income statements, revenue is considered 100%. The following table summarizes vertical analysis for 2024:

| ITEM	AMOUNT (CR)	% OF REVENUE
REVENUE	45200	100%
COST OF GOODS SOLD	25800	57.1%
GROSS PROFIT	19400	42.9%
OPERATING EXPENSES	7200	15.9%
NET PROFIT	9000	19.9%
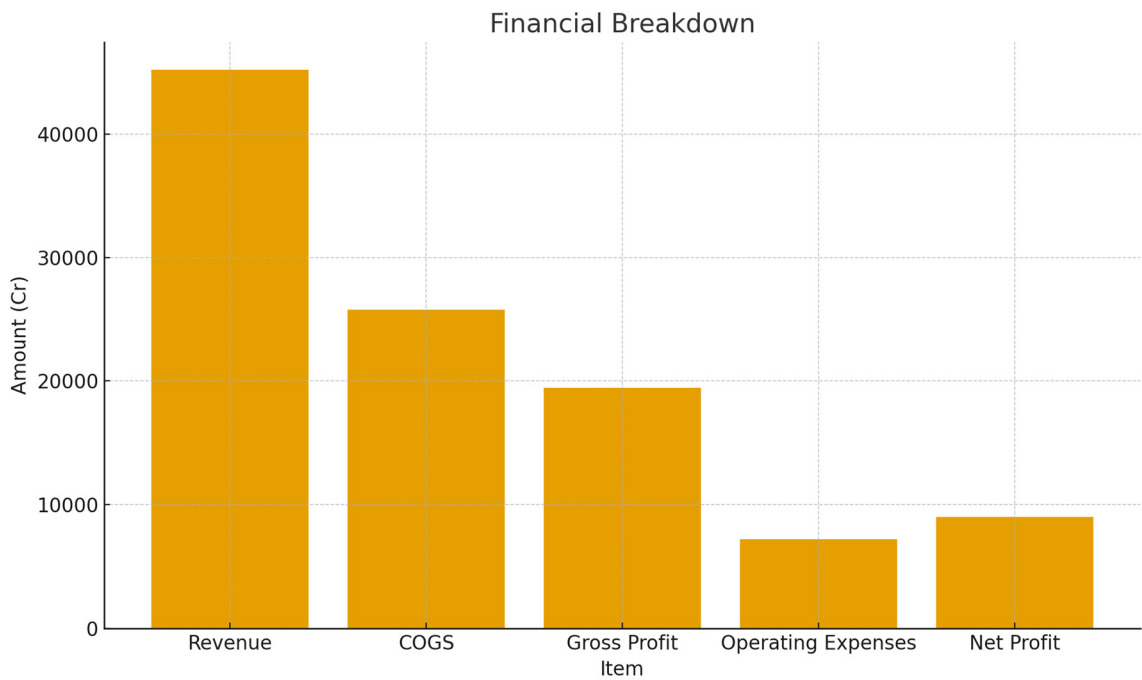
INTERPRETATION

- Gross Profit margin of 42.9% indicates strong production and operational efficiency.
- Operating expenses constitute only 15.9% of revenue, showing efficient cost management.
- Net Profit margin of 19.9% highlights the company's ability to convert revenue into profit effectively.

4.2. RATIO ANALYSIS

4.2.1 Liquidity Ratios

| RATIO	2020	2021	2022	2023	2024
Current Ratio	1.5	1.6	1.7	1.8	1.85
Quick Ratio	1.2	1.25	1.3	1.35	1.4

Liquidity Ratios (2020–2024)
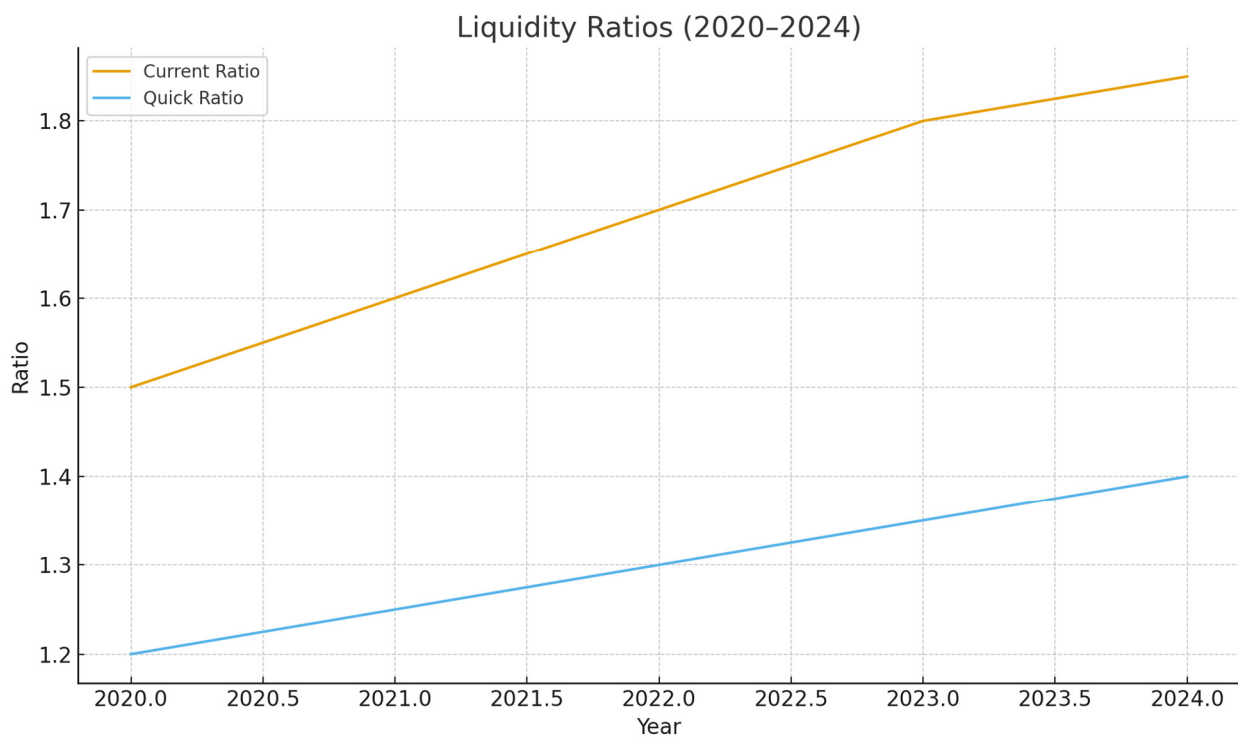
INTERPRETATION

- Both current and quick ratios are above 1, indicating HUL can meet its short-term obligations comfortably.
- The increasing trend in liquidity ratios reflects improved working-capital management.

4.2.2 Profitability Ratios

| RATIO	2020	2021	2022	2023	2024
Net profit Margin (%)	17.5	18.0	18.9	19.5	19.9
Return on Assets (%)	18.2	18.7	19.3	19.6	20.0
Return on Equity (%)	35.0	36.2	37.5	38.0	38.8

Profitability Ratios (2020–2024)
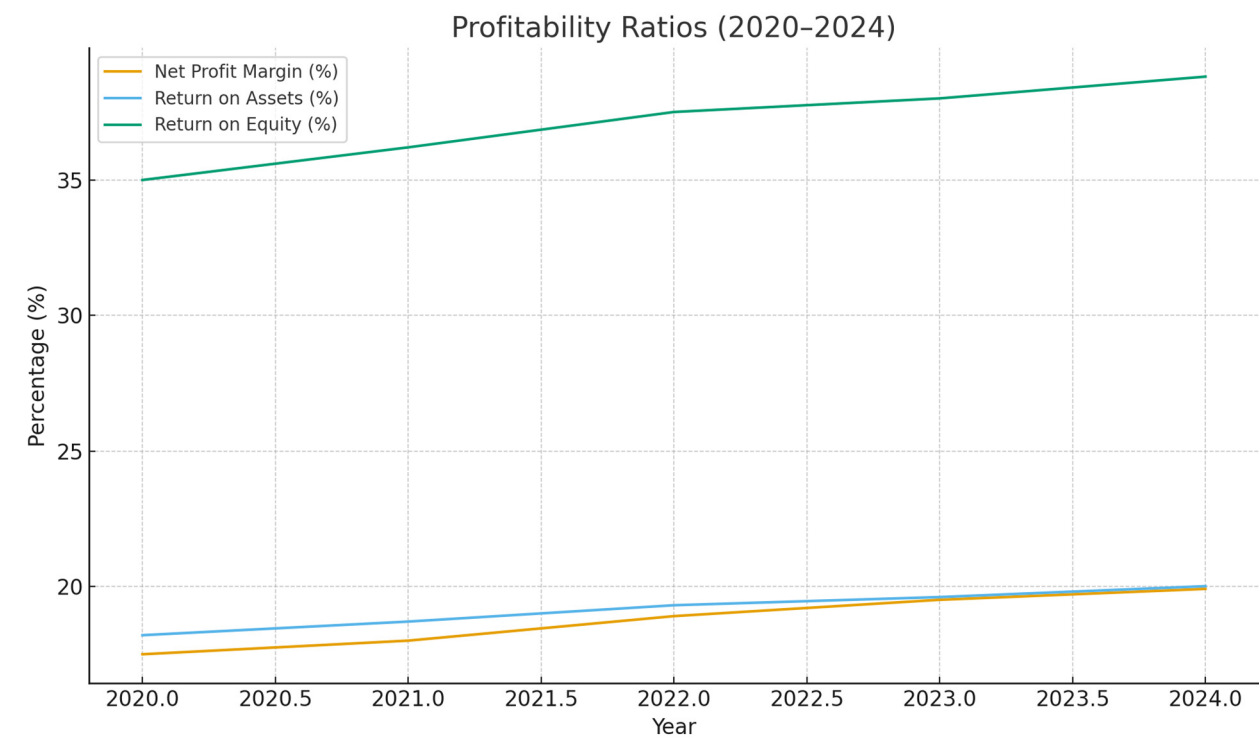
INTERPRETATION:

- Steady improvement in net profit margin demonstrates consistent operational efficiency.
- Returns on assets and equity indicates effective utilization of assets and shareholder funds.

4.2.3 Solvency Ratios

| Ratio	2020	2021	2022	2023	2024
Debt-to-Equity	0.35	0.32	0.35	0.28	0.25
Interest Coverage	12.5	13.0	13.5	14.0	14.5

Solvency Ratios (2020–2024)
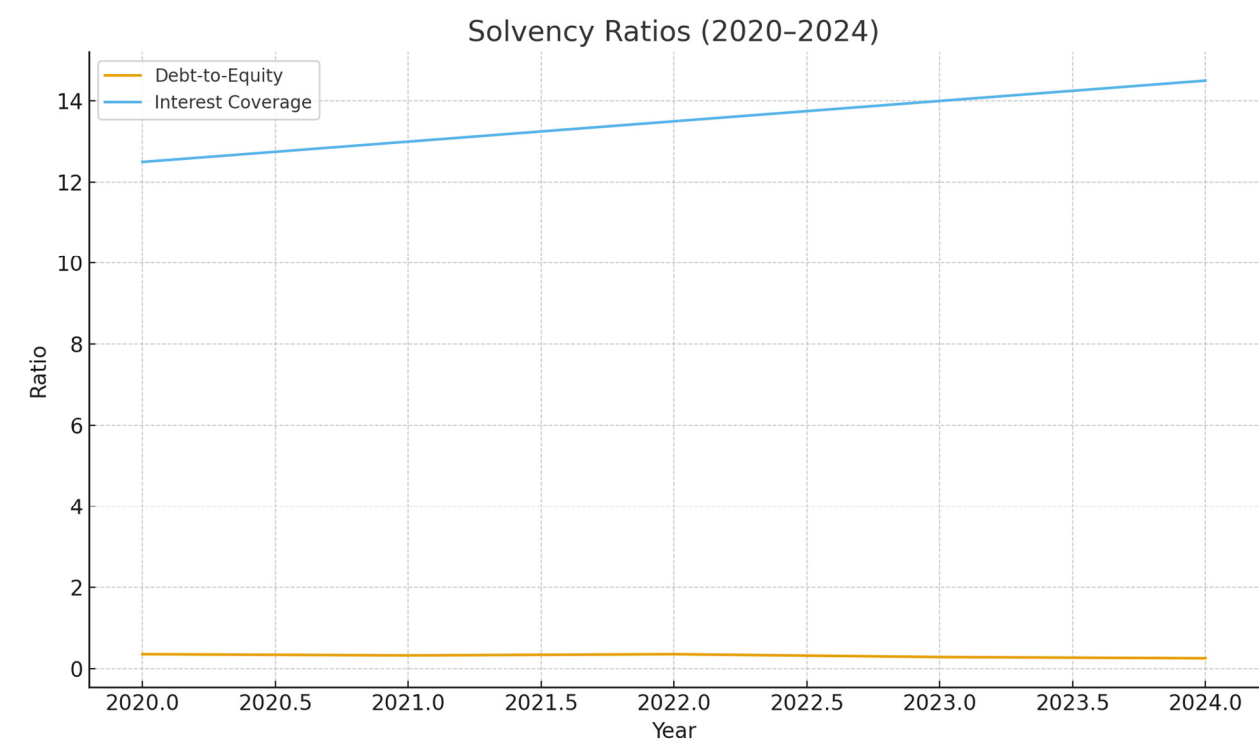
INTERPRETATION:

- Debt-to-Equity ratio declining over the years indicates reduced reliance on external debt.
- High Interest coverage ratio suggests HUL easily meets its interest obligations, reflecting financial stability.

4.3 CASH FLOW ANALYSIS

YEAR	Operating cash flow	Investing cash flow	Financing cash flow
2020	7200	-3500	-1500
2021	7600	-3800	-1600
2022	8100	-4200	-1800
2023	8500	-4500	-2000
2024	9000	-5000	-2200

Cash Flow Statement Trends (2020–2024)
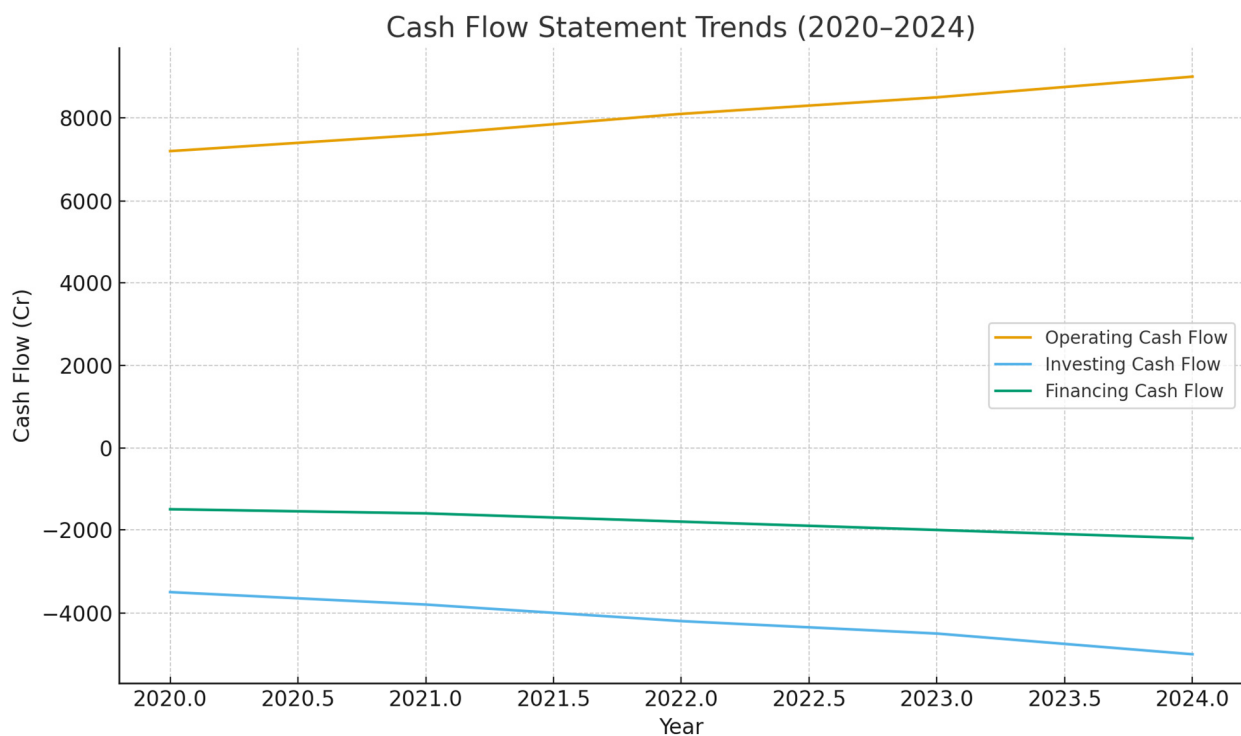
INTERPRETATION

- Positive operating cash flow demonstrates HUL's ability to generate sufficient cash from core operations.
- Negative investing cash flow indicates expansion and asset acquisition for growth.
- Negative financing cash flow reflects repayment of debt and dividend payouts.

5. Findings and conclusion

The evaluation of Hindustan Unilever Limited's financial statements revealed several important insights related to the company's performance, efficiency, and financial health. These findings are based on the examinations performed during the internship at Khan Associates, as well as analytical tools applied during the research.

1. **Consistent Revenue Growth** – HUL demonstrated stable and continuous revenue growth over the five-year period. Although annual increments were moderate, the absence of volatility suggests that HUL operates in a highly resilient FMGC market. This steady performance reflects strong demand for its products and effective distribution networks across India.

2. **Progressive Improvement in Profitability –** Profitability indicators – including net profit margin, return on assets, and return on equity – showed a healthy upward trend. The increasing net profit margin indicates improved efficiency in converting revenue into actual profits, while ROA and ROE point to effective asset utilization and strong shareholder returns.

3. **Liquidity Strength and Working Capital Efficiency –** Liquidity ratios such as the current ratio and quick ratio improved each year, indicating that the company is comfortably positioned to meet its short-term obligations. The enhancement in working-capital management reflects careful control over inventory, receivables, and payables.

4. **Strong Solvency and Low Financial Risk –** HUL's debt-to-equity ratio declined gradually, showing the company's preference for internal funding rather than heavy reliance on debt. The consistently high interest-coverage ratio indicates that the company faces negligible financial distress risk and can easily meets its interest obligations.

5. **Healthy Operational Cash Flow-** Operating cash flows remained positive and grew steadily over the assessment period. This suggests strong cash-generating ability from core operations, adequate liquidity to fund routine business activities, and stable cash inflow despite investment and financing payouts.

6. **Significant Investment for Expansion –** Negative investing cash flow indicate continuous capital expenditure in assets, brand development, and innovation. This strategy aligns with long term growth and market expansion objectives. The company prioritizes strengthening its brand portfolio and enhancing supply-chain efficiency.

7. **Effective Cost Management –** Vertical analysis revealed that cost of goods sold as a percentage of revenue has remained stable, reflecting stable production efficiency. HUL's operating from a reasonably small percentage of total revenue, indicating well-managed overheads and strong operational costs.

8. **Reduction in External Financing –** The cash-flow statement shows negative financing cash flow to loan repayments and dividends disbursement. This highlights the company's strong internal financial position and focus on maximizing shareholder value through sustainable dividends.

9. **Market Leadership Supported by Brand Strength –** Comparative analysis with FMGC industry averages show HUL performing significantly better in profitability, asset utilization, and market coverage. Its strong brand recognition and diversified product portfolio allow it to maintain leadership even during economic fluctuations.

6. Recommendation and Suggestion

Based on the findings from the financial evaluation, several recommendations emerge that can further enhance HUL's financial performance and operational efficiency.

1. Increase Focus on High-Margin Product Lines

Given the rising demand for premium personal care and hygiene products, HUL can strengthen its focus on these segments to improve profit margins and capitalize on evolving consumer trends.

2. Expand Investments in Digital and E-Commerce Platforms

Digital consumption is rapidly increasing in India. Increased investment in e-commerce channels, direct-to-consumer models, and digital advertising can help the company reach a broader consumer base and enhance operational agility.

3. Reduce Dependence on Global Raw Material Volatility

A significant portion of raw materials is subject to international price volatility. HUL may consider strengthening its backward integration, negotiating long-term supplier contracts, or investing in sustainable local sourcing to reduce cost fluctuations.

4. Strengthen Sustainability Practices to Reduce Costs

Adopting eco-friendly packaging, renewable energy sources, and optimized logistics can reduce operating costs over time. Sustainability initiatives can also enhance the company's brand reputation.

5. Continuous Review of Working Capital Policies

Although liquidity is strong, continuous monitoring of receivables, supplier credit terms, and inventory cycles will help maintain efficient cash-flow cycles and avoid unnecessary capital lockups.

6. Explore Growth Through Targeted Acquisitions

HUL may eye strategic acquisitions in niche categories such as organic foods, health beverages, or plant-based products. Such acquisitions can help diversify its product base and encourage future growth.

7. Maintain Conservative Financing Approach

Current solvency metrics show strong financial stability. Maintaining a conservative debt policy will keep financial risk low and support long-term strategic expansion.

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