

## **A Nexus Between Liquidity-Profitability in Bangladesh Pharmaceutical Industry**

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### **ABSTRACT**

This study has investigated the nexus between liquidity and profitability in all quoted pharmaceutical companies in Bangladesh. The primary aim of this study was to investigate the correlation and magnitude of the relationship between profitability and liquidity in profit-driven quoted firms. Additionally, the research sought to ascertain the cause-and-effect relationship between these two performance indicators. We employed investigative and quantitative analysis methods for the study and considered the Current Ratio (CR) as a measure of Liquidity and Return on Asset (ROA) as a measure of profitability. Fifteen quoted pharmaceutical companies were analyzed using information extracted from their annual reports and financial statements for the study period (2017 to 2022). We tried to figure out how much liquidity of a company can explain its profitability. We employed linear regression to find out the extent of relationship between liquidity and profitability (significance level was 10%) of pharmaceutical companies in Bangladesh. We showed graphically how liquidity and profitability of these companies varied over the last couple of years. Finally, based on the findings it was concluded that there is no statistically significant correlation between liquidity and profitability within the listed pharmaceutical firms in Bangladesh.

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### **1. Introduction**

Bangladesh has witnessed rapid growth in its pharmaceutical industry, which is recognized as one of the leading industries for generating revenue for the Government's exchequer. It has experienced accelerated growth in terms of profit, especially during the years 2015-2020 (The Daily Star, 2022), and is considered the most dynamic and powerful industrial entity in Bangladesh. Technologically, it is one of the most

developed manufacturing industries and currently contributes immensely to the total GDP, with great potential for diversification. As the industry grows, understanding the intricate relationship between liquidity and profitability becomes essential for stakeholders aiming to optimize financial strategies and drive long-term success. However, there has been a lot of agreement and disagreement among managers, analysts, experts, and researchers about the tradeoff between liquidity and profitability. In such a context, evaluating the financial health of pharmaceutical enterprises, we have opted to consider the relationship between liquidity and profitability as a cornerstone of this study.

Given this backdrop, a company must manage its liquid assets properly to meet its short-term obligations. Otherwise, inadequate liquid assets may result in insolvency, which could lead to severe financial distress. This situation highlights the critical importance of effective liquidity management, as it ensures that the company can meet its immediate liabilities and maintain operational stability. Through liquidity analysis, one can understand whether a company has enough cash or cash-equivalent assets. To avoid liquidity shortages, companies must maintain adequate cash balances and adhere to effective policies and strategies for an efficient liquidity position (Bharatbhai et al., 2021). Moreover, this approach is vital as profitability, which measures how much a firm's revenues exceed its expenses, is the primary goal of any business organization (Niresh, 2012). It requires proper allocation of resources, typically through employing procedures and establishing rules to manage non-current assets profitably (Jagtap, 2021).

Building on this understanding, effective liquidity management is considered crucial for pharmaceutical companies to sustain their operations and invest in innovative projects. According to Hossain & Kabir (2016), a strong liquidity position allows firms to respond flexibly to unexpected financial demands and capitalize on emerging opportunities. Conversely, profitability ensures that these investments generate sufficient returns to support ongoing operations and strategic goals. Rodriguez et al. (2023) emphasize that while high profitability can indicate successful market positioning and operational efficiency, it must be balanced with adequate liquidity to avoid financial challenges.

Considering these insights, firms in Bangladesh's burgeoning pharmaceutical industry must adeptly manage these financial metrics to achieve long-term success. The ability to balance liquidity and profitability influences not only a company's financial stability but also its capacity to innovate and expand in a competitive global market. Thus, understanding and optimizing the relationship between these financial dimensions is essential for stakeholders seeking to navigate the complexities of the industry and securing a competitive edge.

In light of these considerations, this study aims to investigate the liquidity and profitability relationship of selected pharmaceutical companies in Bangladesh over a six-year period. It is organized into nine sections. Following the introduction, the second section reviews related previous studies. Sections three and four outline the study's objectives and research hypotheses, respectively. Section five details the methodology. Sections six and seven present model specification, data analysis, and findings. Section eight discusses the findings, and section nine concludes the study.

## **2. Relevant Literature Review**

The pharmaceutical industry in Bangladesh has experienced significant growth over the past decades, contributing substantially to the national economy (Hamid, n.d.; Sharif & Islam, 2018). Understanding the dynamics between liquidity and profitability within this sector is crucial for stakeholders, including investors, policymakers, and business managers. Liquidity, often measured by ratios such as the current ratio and quick ratio, indicates a company's ability to meet short-term obligations. Profitability, typically assessed through metrics like return on assets (ROA) and return on equity (ROE), reflects a firm's ability to generate earnings relative to its expenses and other costs. This literature review aims to explore the existing body of research on the relationship between liquidity and profitability, focusing on the pharmaceutical industry in Bangladesh (Padachi, 2006; Quayyum, 2011; Qurashi & Zahoor, 2017)

To begin with, the trade-off theory and pecking order theory provide a foundation for understanding the relationship between liquidity and profitability (Padachi, 2006; Quayyum, 2011; Qurashi & Zahoor, 2017). The trade-off theory suggests that firms balance the costs and benefits of

holding liquid assets (Myers, 1984), while the pecking order theory posits that companies prioritize their sources of financing based on the principle of least effort or resistance, starting with internal funds (Myers & Majluf, 1984). These theories help elucidate why firms might hold different levels of liquidity and how this affects their profitability.

Building on these theoretical foundations, several empirical studies have examined the relationship between liquidity and profitability across various industries and regions. Generally, findings indicate a mixed relationship, with some studies reporting a positive correlation and others a negative or insignificant relationship. For instance, Eljelly (2004) investigated the relationship between liquidity and profitability in Saudi Arabia, finding that liquidity significantly affects profitability. Specifically, the study noted a negative relationship between the current ratio and profitability indicators. Similarly, Raheman and Nasr (2007) conducted a study on Pakistani firms and observed a significant negative relationship between liquidity and profitability, suggesting that excessive liquidity might reduce profitability due to the opportunity cost of holding liquid assets.

Furthermore, Uyar (2009) examined Turkish companies and found that efficient liquidity management positively impacts profitability, highlighting the importance of maintaining optimal liquidity levels. Likewise, Ajanthan (2013) focused on the Sri Lankan hotel industry and discovered a positive relationship between liquidity and profitability, suggesting that higher liquidity provides firms with the ability to seize investment opportunities and improve profitability.

Moreover, research specifically targeting the pharmaceutical industry provides more nuanced insights into the liquidity-profitability nexus. For example, Lazaridis and Tryfonidis (2006) studied the Greek pharmaceutical sector and reported a positive relationship between liquidity and profitability. They argued that adequate liquidity enables firms to sustain operations and invest in research and development, driving long-term profitability. Similarly, Gill, Biger, and Mathur (2010) investigated the relationship between liquidity and profitability in the pharmaceutical sector in the United States, finding that firms with higher liquidity levels tend to achieve better profitability metrics due to their ability to manage operational risks effectively.

In the context of Bangladesh, the pharmaceutical industry, being one of the fastest-growing entities, has garnered significant academic attention. Given the pivotal role of the pharmaceutical industry in Bangladesh's economy and public health infrastructure, it is imperative to understand the specific dynamics of liquidity and profitability within this industry. However, studies focusing on the liquidity-profitability relationship within this sector remain limited. To better understand the current state of research, it's important to examine the findings from the few studies that have explored the liquidity-profitability relationship in Bangladesh's pharmaceutical industry. These studies offer varied perspectives, highlighting both the complexities and the gaps that still exist in this area of research. For instance, one study found no significant relationship between liquidity and profitability in the pharmaceuticals and chemicals sector of Bangladesh (Hamid & Akhi, 2016). Another study on Square Pharmaceuticals Ltd. indicated that while the company maintains a satisfactory level of profitability, its liquidity and inventory turnover ratios are not up to standard, indicating potential financial risks (Rahman, 2014). Further research revealed that liquidity had no significant impact on profitability, while solvency showed a statistically significant relationship with profitability in Bangladesh's pharmaceutical and chemical sectors (Hamid, 2023). These findings highlight the critical need for more targeted research to fully understand the financial dynamics at play in this essential industry in Bangladesh.

However, while there is substantial research on the relationship between liquidity and profitability across different regions and industries, the findings are often mixed and inconclusive. For instance, while some studies report a positive relationship, others find a negative or insignificant correlation. However, the pharmaceutical industry in Bangladesh, despite its significant economic role, remains underexplored in this context. This study aims to fill this research gap by providing a detailed analysis of the liquidity-profitability dynamics within this crucial sector, thereby offering valuable insights for stakeholders and contributing to more effective financial management practices.

### **3. Objectives of the study**

This study aims to investigate the liquidity and profitability relationship of selected pharmaceutical companies in Bangladesh over a considerable period and the main objectives of this study are to:

- i. To determine the relationship between liquidity and profitability of pharmaceutical companies in Bangladesh
- ii. To measure the nature and extent of the relationship between liquidity and profitability.

#### **3.1 Research Hypotheses:**

The following hypotheses are being considered to examine the nexus between profitability and liquidity within the pharmaceutical industry in Bangladesh.

##### **Hypothesis One:**

**H0:** Liquidity and profitability have no impact on each other in pharmaceutical companies.

**H1:** Liquidity and profitability have an impact on each other in pharmaceutical companies.

##### **Hypothesis Two:**

**H0:** There exists no relationship between liquidity and profitability in pharmaceutical companies.

**H1:** There exists a relationship between liquidity and profitability in pharmaceutical companies.

### **4. Methodology of the Study**

#### **4.1 Research Design**

Research has been conducted based on secondary data using the quantitative research method.

#### **4.2 Source of Data and Study Period**

Data relating to the study were obtained from the annual reports of the selected companies. In addition, journals and books were also used to gather relevant necessary information. The study covered a period of 6 years starting from 2017 to 2022 based on the consideration of the availability of data.

**4.3 Sample Size and Selection**

We selected 15 listed pharmaceutical companies irrespective of their size to see the extent to which they were profitable financially. A purposive sampling technique was adopted in this context. Among all the pharmaceutical companies in Bangladesh, we mainly focused on those who are enlisted in the Dhaka Stock Exchange. It was assumed that the financial statements of listed companies were more reliable than those of non-listed ones. Correlation and regression analyses were employed as statistical tools to facilitate the analysis and interpretation of the relevant data.

**4.4. Reassessment of Research Hypotheses**

The previously stated hypotheses form the basis for analyzing and concluding the relationship between liquidity and profitability. To evaluate the first hypothesis, a correlation analysis is conducted to examine the strength and direction of the relationship between liquidity metrics and profitability indicators. For the second hypothesis, regression analysis is employed to assess how variations in liquidity metrics influence changes in profitability within the pharmaceutical sector in Bangladesh.

**4.5 Model Specification**

To empirically examine and analyze the proposed dual relationship between liquidity and profitability, simple regression models were established. These models theoretically suggest that liquidity (LQTY) is influenced by profitability (PFTY), and, in turn, profitability (PFTY) is influenced by liquidity (LQTY). This relationship can be functionally represented as:

$$\begin{aligned} \text{LQTY} &= f(\text{PFTY}) \dots\dots\dots \text{I} \\ \text{PFTY} &= f(\text{LQTY}) \dots\dots\dots \text{II} \end{aligned}$$

Based on these functional relationships, the following simple regression models are specified:

$$\begin{aligned} \text{LQTY} &= \beta_0 + \beta_1\text{PFTY} + \mu \dots\dots\dots \text{I} \\ \text{PFTY} &= \lambda_0 + \lambda_1\text{LQTY} + \mu \dots\dots\dots \text{II} \end{aligned}$$

Where,  
 $\lambda_0$  and  $\beta_0$  represent the intercepts of the regression lines,

$\beta_1$  and  $\lambda_1$  are the slope coefficients indicating the nature and impact of the relationship between the variables,  
 $\mu$  is the stochastic term accounting for the influence of other factors affecting liquidity and profitability that are not included in the model.

## 5. Data Analysis & Findings

In the context of the study's objectives, first, an attempt was made to find out the relationship between liquidity and profitability of the sample pharmaceutical enterprises. To this end, the correlation coefficient between liquidity (CR) and profitability (ROA) was computed. The following table shows the result:

### 5.1 Correlation Analysis Result

The initial phase of the analysis investigates the correlation between liquidity, measured by the Current Ratio (CR), and profitability, measured by Return on Assets (ROA), within the pharmaceutical enterprises. The correlation coefficient was computed, yielding the following results:

Table-1: Correlation Analysis

Correlations		CR	ROA
CR	Pearson correlation	1	0.152
	Sig. (2-tailed)		0.150
	N	91	91
ROA	Pearson correlation	.152	1
	Sig. (2-tailed)	.150	
	N	91	91

(Source: SPSS Analysis, 2024)

From the analysis, it is observed that there is a very weak positive correlation (0.152) between CR (liquidity) and ROA (profitability), and this correlation is not statistically significant ( $p = 0.150$ ). Therefore, the relationship between ROA and CR is weak and negligible based on these results.

### 5.2 Regression and Coefficient Analysis

- i) Considering the negligible and poor correlation between ROA and CR, regression analysis was attempted (for model-I) as a more



extensive evaluation. The regression analysis result is depicted in the following table.

**Formula:**  $PFTY = f(LQTY)$ .....I

Table-2: Regression Analysis

Metric	Value
Multiple R	0.142
R Square	0.020
Adjusted R Square	0.009
Standard Error	0.112
Observations	89

Source: SPSS Analysis, 2024

Table-3: ANOVA

Source	df	SS	MS	F	Significance F
Regression	1	0.0227	0.0227	1.7937	0.1840
Residual	87	1.1008	0.0127		
Total	88	1.1235			

Source: SPSS Analysis, 2024

Table-4: Coefficients Analysis

Variable	Coefficient	Standard Error	t-statistic	P-value	Lower 90.0%	Upper 90.0%
Intercept	0.0391	0.0160	2.4401	0.0167	0.0125	0.0658
LQTY	0.0038	0.0029	1.3393	0.1840	0.0009	0.0086

Source: SPSS Analysis, 2024

The value of the R-square is 2%, indicating that only a very small portion of profitability can be explained by liquidity. Furthermore, the regression model's p-value of 0.1840, which is greater than 0.10, indicates that it is not statistically significant, implying that liquidity is not a strong predictor of profitability.

- ii) Again considering the negligible and poor correlation between profitability and liquidity, regression analysis was attempted (for

model-II) as a more extensive evaluation. The regression analysis result is depicted in the following table.

**Formula:**  $LQTY=f(PFTY)$ .....II

Table-5: Regression Analysis

Metric	Value
Multiple R	0.142
R Square	0.020
Adjusted R Square	0.009
Standard Error	0.112
Observations	89

Source: SPSS Analysis, 2024

Table-6: ANOVA

Source	df	SS	MS	F	Significance F
Regression	1	31.383	31.383	1.7937	0.1840
Residual	87	1522.196	17.497		
Total	88	1553.579			

Source: SPSS Analysis, 2024

Table-7: Coefficients Analysis

Variable	Coefficient	Standard Error	t-statistic	P-value	Lower 90.0%	Upper 90.0%
Intercept	3.4753	0.4911	7.0769	3.56E-10	2.6589	4.2917
PFTY	5.2853	3.9463	1.3393	0.1840	2.6589	11.8463

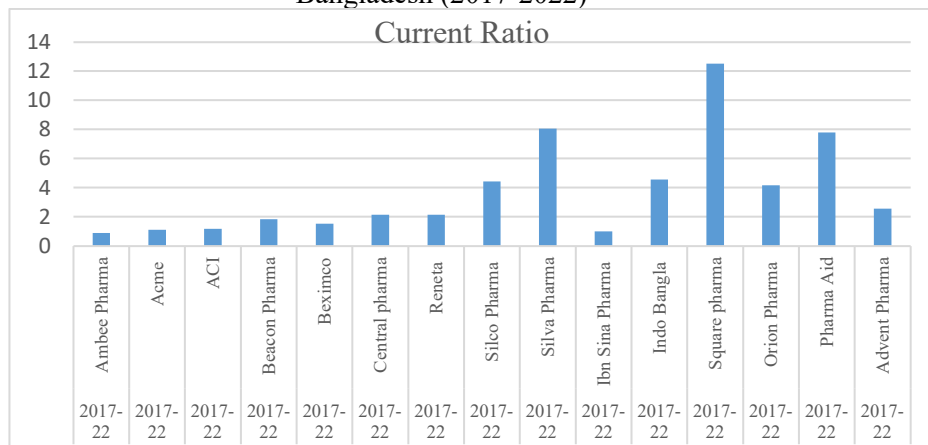
Source: SPSS Analysis, 2024

The value of R-square remains at 2%, and the p-value stands at 3.56E-10 (0.000000000356), which is smaller than the conventional value of 0.10. The results indicate that only 2% of the liquidity is explained by profitability. Despite the low R-square value, the p-value (3.56E-10) for the intercept is significant, but the overall model is not, suggesting that while there is some relationship between the variables, it is not strong or predictive enough to be considered significant.

### 6. Discussion

The results of this study reveal that there is no significant relationship between liquidity (measured by the current ratio) and profitability (measured by ROA) among pharmaceutical companies in Bangladesh. The weak positive correlation (0.152) between liquidity and profitability is not statistically significant ( $p = 0.150$ ), highlighting a negligible relationship. Moreover, the R-square value of 2% suggests that only a small portion of profitability is explained by liquidity. Despite a notable p-value of 0.016714, which suggests some level of association between profitability and liquidity, the regression model is not statistically significant ( $p = 0.1840$ ). This further underscores that liquidity is not a strong predictor of profitability in the pharmaceutical sector. Thus, all the models used in the analysis show only a minimal degree of dependency, with no significance at the 10% level.

Figure 1: Current Ratio of Different Pharmaceutical Companies in Bangladesh (2017-2022)

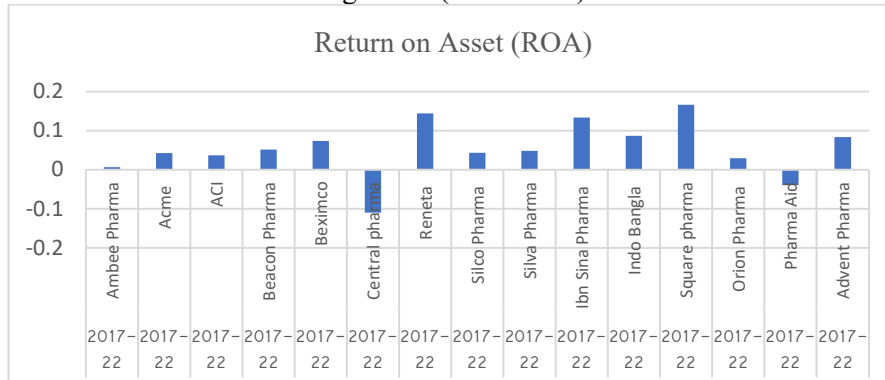


Source: Researchers' own Illustration using data extracted from the Annual Reports (2017-2022)

We also laid out the current ratio data for various pharmaceutical companies in Bangladesh from 2017 to 2022, as shown in Figure 1. Companies like Square Pharma consistently maintain a strong current ratio, indicating stable liquidity, while others like Ambee Pharma and Ibn Sina Pharma show weaker liquidity and more variability. In parallel, the profitability trends illustrated in Figure 2 reveal that Square Pharma and Beximco display relatively high ROA, reflecting efficient asset

utilization, whereas Central Pharma and Pharma Aid struggle with low or negative ROA. This variation in profitability across companies helps explain the lack of a significant relationship between liquidity and profitability in the sector.

Figure 2: Return on Assets of Different Pharmaceutical Companies in Bangladesh (2017-2022)



Source: Researchers' own Illustration using data extracted from the Annual Reports (2017-2022)

In brief, this study's findings of a weak and insignificant correlation between liquidity (CR) and profitability (ROA) are consistent with the results reported by Hamid and Akhi (2016), who also observed minimal impact of liquidity on profitability in the pharmaceutical sector. Their research demonstrated positive correlations between certain liquidity measures (quick ratio and working capital ratio) and profitability measures (ROA and ROE), but a negative association with the current ratio. Taken as a whole, both studies suggest that liquidity is not a strong predictor of profitability, with only 2% of profitability variability explained by liquidity.

### 7. Conclusion

This study has underscored the importance of understanding the relationship between liquidity and profitability in the pharmaceutical sector in Bangladesh, revealing a weak correlation between liquidity, as measured by the current ratio, and profitability, as measured by return on assets. Although Bangladesh hosts over thirty-five pharmaceutical companies, not all are listed on the Dhaka Stock Exchange. It is essential for every organization to maintain an optimal balance between liquidity

and profitability. We would like to conclude by emphasizing that every organization should maintain an optimal balance between liquidity and profitability. Liquidity is crucial for ensuring that a firm can meet its short-term obligations, and this can only be sustained through profitable operations. Therefore, the dual objectives of profitability and liquidity must be effectively managed. Looking ahead, future research should consider additional variables and expand the scope to include the broader pharmaceutical and chemical industries for a more comprehensive analysis.

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**Appendix-1**

**Table: Current Ratio (CR) and Return on Asset (ROA)**

Year		2017	2018	2019	2020	2021	2022
Company Name	Ratio						
Ambee Pharma	Current Ratio	0.88442199	0.888653	0.87531813	0.89197385	0.87432316	0.92083816
	ROA	0.01606513	0.01861738	0.00835499	0.00849601	-0.0308715	0.0159859
ACME	Current Ratio	1.25295521	1.10599621	0.93352338	1.05176202	1.1440919	1.12342225
	ROA	0.0466771	0.04372732	0.04009785	0.03679761	0.03876891	0.04911914
Beacon	Current Ratio	2.13063135	1.80092985	2.02568707	1.843467	1.86767867	1.3786977
	ROA	0.02031631	0.02569121	0.02416352	0.053044	0.10115518	0.08646416
ACI	Current Ratio	1.29085386	1.1718692	1.12568102	1.11640103	1.16774133	1.18610547
	ROA	0.04596104	0.03691669	0.01304164	0.03884154	0.04612045	0.04016767
Central pharma	Current Ratio	3.24505931	3.3072801	2.75779879	0.95601787	1.36523014	1.25183566
	ROA	0.04762662	0.02563914	0.02308621	-0.8166898	0.00620612	0.05203813
Reneta	Current Ratio	1.75162635	2.2170333	2.67469346	2.52603671	2.2867565	1.38467821
	ROA	0.1441234	0.15361329	0.1579821	0.14218141	0.14643486	0.12164434
Silco Pharma	Current Ratio	4.27366112	4.29582271	5.55562919	5.09790593	3.71864006	3.60509106
	ROA	0.0517187	0.04909077	0.06326601	0.03128467	0.03140218	0.03105126
Beximco	Current Ratio	2.68077221	1.33786679	1.07545868	1.17011078	1.47906028	1.40350539
	ROA	0.06532938	0.06068944	0.06326256	0.06909235	0.09718905	0.08646245
Silva Pharma	Current Ratio	5.29304173	4.56814386	11.8151036	6.82123957	12.1483658	7.69791171
	ROA	0.0413559	0.04645616	0.06226789	0.04842545	0.04897677	0.04018311
Ibn Sina	Current Ratio	0.885821	0.80916014	0.84262465	0.80986551	1.19905853	1.45112895
	ROA	0.10851447	0.18523567	0.11888641	0.11558985	0.12903791	0.14198526
Indo Bangla	Current Ratio	5.3111456	4.85303761	5.31461388	4.8244965	3.57275113	3.49479681
	ROA	0.12615918	0.1242076	0.09788864	0.0898331	0.07125294	0.0132929
Square Pharma	Current Ratio	6.35228514	4.90931677	12.9307805	14.5246892	17.6677545	18.7359538
	ROA	0.17027851	0.15412773	0.16235155	0.17425465	0.17024086	0.16832383
Orion Pharma	Current Ratio	2.21927274	2.28287524	4.20469422	4.88549611	6.13699471	5.21409819
	ROA	0.00837428	0.00976678	0.0499334	0.03438218	0.04218527	0.02943566
Pharma aids	Current Ratio	4.07200548	3.29589443	21.3928857	15.4672404	1.47458257	1.09298162
	ROA	0.05428768	-0.2977786	-0.0204588	0.0039646	0.0100237	0.01306154
Advent Pharma	Current Ratio	2.96783786	4.5421625	2.68679641	2.00550807	1.72001255	1.38347147
	ROA	0.06694814	0.08578232	0.13116728	0.08533047	0.07472806	0.05933685

*Source: Annual Reports of the listed Companies (2017-2022)*

**Declaration of Interests**

*We, the authors of this research manuscript, declare that we have no financial interest. We have provided written consent to publish the paper in this journal.*

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