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PROFITABILITY RATIO ANALYSIS AS A TOOL FOR PERFORMANCE MEASUREMENT: A CASE STUDY OF DIGITECH SOLUTIONS

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Abstract

This paper evaluates the financial performance of Digitech Solutions, Bathinda over a span of five years through profitability ratio analysis. Key ratios, including the Gross Profit Ratio, Operating Profit Ratio, Net Profit Ratio, Profit Before Tax Margin, Quick Ratio, and Current Asset Turnover Ratio, were applied to measure the firm's profitability, liquidity, and operational efficiency. The results indicate that although the company demonstrates strong liquidity and consistent net profitability, both its operating profit and profit before tax margins exhibit a downward trend, posing potential risks to long-term sustainability. To address these concerns, the study suggests measures such as minimizing operational expenses, enhancing asset utilization, and channeling idle resources into productive investments. Ultimately, the research highlights how profitability ratio analysis serves as a vital link between theoretical financial principles and their real-world application in business decision-making.

Keywords: Profitability Analysis, Ratio Analysis, Financial Performance, Liquidity, Net Profit, Operating Profit, Quick Ratio, Current Asset Turnover, Digitech Solutions, Financial Management

1. Introduction

Profitability is universally recognized as one of the most critical parameters of financial performance, as it directly reflects a firm's ability to generate returns from its resources. A business that consistently earns profits not only ensures its survival but also secures long-term growth, competitiveness, and sustainability in an increasingly dynamic market environment. Profitability analysis is thus central to financial management, as it assists managers, investors, and policymakers in evaluating operational efficiency, investment potential, and shareholder value creation. Financial ratio analysis, particularly profitability ratios, provides a structured approach to examining how effectively a company converts sales and assets into net earnings. Ratios such as Gross Profit Ratio, Operating Profit Ratio, Net Profit Ratio, Profit Before Tax Margin, Quick Ratio, and Current Asset Turnover Ratio serve as diagnostic tools that highlight both the strengths and weaknesses of a firm's financial position. When analyzed over time, these ratios reveal performance trends and help predict future sustainability. This study focuses on Digitech Solutions, Bathinda, a company operating in the technology-driven service sector. Given the rapid pace of digital transformation and increasing competition in the IT and service industry, analyzing the financial health of firms such as Digitech Solutions becomes highly relevant. The research examines the company's financial performance over a five-year period (2020–21 to 2024–25) using a set of profitability and efficiency ratios. The aim is to assess whether the firm has been able to maintain consistent profitability, liquidity, and operational effectiveness in the face of evolving business challenges.

2. Review of Literature

Kumar & Sharma (2022) investigated IT and technology companies in India and reported that asset utilization efficiency and capital structure decisions are strongly associated with profitability ratios like ROA and ROE.

Altaf & Ahmad (2023) studied liquidity–profitability relationships in emerging markets and concluded that while liquidity is essential for solvency, excessive liquidity may reduce profitability if funds remain idle.

Smith et al. (2024) in a systematic review of manufacturing industries highlighted that internal factors such as innovation, sustainability practices, and governance structures play a more significant role in driving profitability than external macroeconomic variables.

Rao & Verma (2024) conducted a comparative study of FMCG firms in India and found considerable variation in profitability ratios across companies, attributing the differences to strategic choices, cost efficiency, and market positioning.

3. Objectives of the Study

To assess the profitability performance of Digitech Solutions.

4. Scope of the Study

The scope of this research is limited to the financial analysis of Digitech Solutions over five financial years. It involves examining profitability, liquidity, solvency, and efficiency ratios using financial statements. The study excludes qualitative factors like employee morale or market risks. Findings benefit management, employees, and investors.

5. Research Methodology

Design: Descriptive research design
Data Sources: Primary (interviews with finance heads) and Secondary (annual reports, balance sheets)
Period of study: FY 2020–21 to FY 2024–25.
Tool of Analysis: Ratio analysis
Limitations: Dependence on historical data and exclusion of qualitative aspects

6. Data Analysis

The below table show the different ratios from FY 2020–21 to FY 2024–25:

Year	Gross Profit Ratio (%)	Operating Profit Ratio (%)	Net Profit Ratio (%)	PBT Margin (%)	Quick Ratio	Current Asset Turnover
2020-21	9.05	8.4	8.41	10.43	1.40	0.95
2021-22	9.31	7.35	7.34	9.90	1.27	0.98
2022-23	9.34	8.57	9.23	11.37	1.24	0.95
2023-24	7.79	7.38	8.18	8.56	1.14	0.87
2024-25	10.07	3.73	15.73	6.16	1.42	0.72

Interpretation - The analysis shows that the Gross Profit Ratio fluctuated over the period, falling to **7.79% in 2023–24** before recovering strongly to **10.07% in 2024–25**, suggesting some improvement in cost control. In contrast, the Operating Profit Ratio recorded a worrying decline, dropping sharply from **8.40% in 2020–21** to just **3.73% in 2024–25**, indicating rising operating expenses that may weaken long-term profitability. Interestingly, the Net Profit Ratio improved substantially from **8.41% in 2020–21** to **15.73% in 2024–25**, reflecting effective handling of non-operating income or reduced tax liability, though this gain is not aligned with declining operating efficiency. The PBT Margin peaked at **11.37% in 2022–23** but declined to **6.16% in 2024–25**, showing pressure from costs and taxes in the later years. Liquidity remained strong throughout, with the Quick Ratio staying above 1, reaching **1.42 in 2024–25**, which confirms the firm's ability to meet short-term obligations. However, the Current Asset Turnover gradually fell from **0.98 in 2021–22** to **0.72 in 2024–25**, highlighting inefficiency in asset utilization and the risk of funds being tied up in idle resources.

7. Findings

- The Gross Profit Ratio showed fluctuations, dropping to 7.79% in 2023–24 but improving to 10.07% in 2024–25, indicating unstable cost management.
- The Operating Profit Ratio declined consistently, reaching a low of 3.73% in 2024–25, which reflects rising operating and administrative expenses.
- The Net Profit Ratio rose sharply to 15.73% in 2024–25 despite falling operating margins, suggesting that profitability was supported more by non-operating incomes or tax benefits rather than core operations.
- The PBT Margin showed a downward trend after 2022–23 (11.37%), falling to 6.16% in 2024–25, which may undermine long-term sustainability.

- Liquidity remained healthy, with the Quick Ratio consistently above 1, reaching 1.42 in 2024–25, ensuring strong short-term solvency.
- The Current Asset Turnover ratio declined steadily from 0.98 in 2021–22 to 0.72 in 2024–25, pointing toward inefficiency in asset utilization and potential locking of funds in idle assets.

8. Suggestions

- The company should adopt cost control strategies to reduce administrative and operating expenses, thereby strengthening its Operating Profit Ratio.
- Greater emphasis should be placed on improving operational efficiency rather than relying on non-operating income for profitability.
- Measures such as better working capital management and efficient use of current assets are needed to reverse the declining asset turnover trend.
- The management should consider reinvestment of idle funds into productive ventures to enhance returns and support growth.
- Regular monitoring of profitability and liquidity ratios is recommended for early identification of weaknesses and timely corrective actions.
- Strategic steps like diversification, technology adoption, and process optimization can help the company sustain profitability in a competitive environment.

9. Conclusion

The financial performance analysis of Digitech Solutions, Bathinda over the five-year period (2020–21 to 2024–25) highlights both strengths and areas of concern. The company has demonstrated strong liquidity throughout, with the Quick Ratio consistently above 1, ensuring its ability to meet short-term obligations. Net profitability also improved significantly, reaching 15.73% in 2024–25, which reflects the firm's ability to deliver healthy returns to stakeholders. However, the declining trend in the Operating Profit Ratio, which fell to 3.73%, and the Profit Before Tax Margin, which dropped to 6.16%, points toward rising operational costs and inefficiencies in core business activities. In addition, the steady fall in the Current Asset Turnover ratio to 0.72 suggests poor utilization of assets and potential locking of resources in unproductive areas. These issues, if left unaddressed, could undermine long-term sustainability despite short-term profitability gains. Therefore, the study concludes that Digitech Solutions must prioritize cost reduction, strengthen operational efficiency, and improve asset utilization to ensure balanced and sustainable financial performance in the future.

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