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A Review of Impact of Trade Credit on Firm's Profitability: A Study of Non-financial Firms in Pakistan

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Abstract
Business plays an important role in economic growth, which increasingly draws public attention in recent decades. Previous literature discusses the reasons why the companies offer and receive trade credit. However, it lacks empirical evidence to confirm the relationship between trade credit and profitability. This work focuses on how trade credit, from both the supplier side and the demand side, influences the profitability of SMEs. We investigated 100 firms to establish a long-term relationship with their suppliers to gain credits since accounts payable is positively related to the profitability. Meanwhile, I find that there is no clear relationship between accounts receivable and profitability.
Keywords: Trade credit Accounts revivable Accounts Payable Profitability SMEs Transaction theory

INTRODUCTION
Non-financial enterprises play important roles in the economic growth that can draw public attention in last decades. There are different approaches can be used to manage the working capital management in financial growth cycle. Theories and empirical investigations show a clear overview about non-financial (Berger and Udell, 1998). Earlier studies focus on the trade credit which are important to manage the short term finance of firms in the shape of account receivables and account payables. So, the firms can take use of credit in two aspects; by providing the credit sale to its customers and presenting it the balance sheet as debtors in regular market as short term finance. Secondly, the firm can take the credit purchase by its suppliers by putting the accounts payables on the balance sheet in liability side. Empirical data show that over 80% of business-to-business transactions in United Kingdom are made on credit (Tirole, 2006).

Broadly trade credit can be divided into two parts; account receivables and account payables. On the supply crosswise, trade credit is measured as an asset in the terms of versions receivable. There are the subsequent benefits of credit: decreases of operational expenses, increases in sales, the emerging of associate rate on return and the establishing of steady commercial relations with buyers. On the request side, trade credit can be measured as short term arrears in terms of accounts owed. The benefits of trade acclaim are as follow. Firstly, trade credit was efficient approach to speech monetary frictions. Secondly, agreeing to credit limiting theory cannot admittance to the outdated financial system.

Generally it is feel that by providing the trade credit to both the customer and gain by suppliers can enhance the growth and profitability in non-financial firms, but it can be associated with the risk element. As risk lower management or controller can relax the credit policy by providing more loans to their customers but on the other hand risk averter management can strict it down the same policy by choosing the more valuable customers by providing. Here comes another factor that is availability of working capital or cash flows of the firms depending upon the size and business nature of the firms. As in business to business firm have more reliability those others because they are using the same raw materials in some other operation by providing credit to their customers, which increases the dependability of the debtors on the firm. Likewise the account payables provide more relaxation to the company by granting trade credit in the shape of credit purchases. The volume of the credit purchase depends upon the credit policy of the supplier and also on numbers of the suppliers as well as goodwill of the buying firm. Form above discussion we can say that profitability of a firm has magnificent effects of trade credit either it is account receivables or account payables to verify its effects upon non-financial firms in Pakistan. This research work has been conducted to overcome the gap by selecting a sample of non-financial firms in Pakistan. Both accounts payables and account receivables have been studied as trade credit to check the impact on profitability with some constant variables. This research work would be applicable to the non-financial firms across the different sectors in Pakistan.

LITERATURE REVIEW
Morellec and Smith (2006) found the volume for debt volume growth. Leverage and firm's optimal total debt level decline if the firm's worth increases with the surplus growth options. The results of the study showed that there is a negative relation between growth and the leverages and it also provides the interpretation of leverage

regressions. And the limitations were the sample was taken from United States of America between 2000. They take the sample of between the years 1950 to 1999, for the purpose of the research to include the more than 109,000 firm year observations. Schwartz (1974) told the economic modal for trade credit and firm's profitability with growth. He said the buyer's time to plan for the purpose of purchases, which empower the firms to hold credit instead of cash payment and receipts in the shape of credit payables and credit receivables respectively.

Ahmed, Xiaofeng, Virk and Abdullah (2015) during the financial crises of 2008 found that a relationship related to trade credits (payable and receivable) with bank loan, for the purpose the data is collected form Karachi Stock Exchange from the years of 2005 to 2011. The used the technique of Two Stage Least Square (TSLS) estimation and they analyzed that by finding the determents of credit supply and bank loan at the same time. For the purpose of they use fixed effect model for panel data of almost 11040 Portuguese industrial companies, by them 360 are large one and rest of them are of medium or small size and these are in majority in sample percentage. They found that large companies serve financial intermediaries to their customer, and they also suggested that credit is one the most important factor to increase the profitability of the firms (Santos & Silva, 2014).

Atanasova (2007) assumed approach for the usage of trade credit and institutional finance for analyzing the framework to the effect of the availability of institutional loans on the demand of the trade credit. By the use of the research work, he told to give significance trade credit and also showed a relation with loan of institutions. Further in line with studies on the credit channel of monetary policy transmission, he establishes an enlarged trust on trade credit for financially guarded firms.

Ferrando and Mulier (2012) investigated the influence do firms usage the trade credit network to accomplish growth? They used over 2.5 million observations to the purpose of 600 firms in 8 European countries during the period of 1993-2009, and told the firms use the tool of trade credit to manage growth. In such countries somewhere the trade credit frequency for current, and the influence is lesser but the overall impact is greater than specific. At last they found that the total circumstances of the financial market matter for the important of trade credit for the purpose of growth. There is a descriptive study showed the use of collect data from the field of firms in Kenya in manufacturing sector and for the purpose stratified random sampling technique recycled over a model of 81 manufacturing firms. Questionnaire is used to analyze the collected data form 71 manufacturing companies in Nairobi industrial area and environs in Kenya. For the purpose Analysis; ANOVA and regression analysis techniques are used to exam the hypothesis. The results presented that a positive association between profitability and credit policy for the manufacturing firms in Kenya.

Fisman and Love (2003) realized the impact for trades (both account receivables) pay the influence of financial intermediary development as well as industry growth. They also found that industries with larger dependence for trade credit which can make the industries a larger dependence for the trade credit financing which has higher rates of growth in such a countries which have weaker financial institutions. Moreover, with the help of barriers to trade credit access among with existing firms, and they showed that most of effect which can report comes from growth. At last they found that the total circumstances of the financial market matter for the important of trade credit for the purpose of growth. There is a descriptive study showed the use of collect data from the field of firms in Kenya in manufacturing sector and for the purpose stratified random sampling technique recycled over a model of 81 manufacturing firms. The primary consequences variable is a real growth in prized added, projected in the 37 businesses for 43 different countries, and by obtained the data from the General Industrial Statistics.

Vaidya (2011) found factors of trade credit: evidence from Indian manufacturing firms. The work is designed especially for Indian context. The empirical evidence optional the strong evidence which found in the support for inventory management motive. Highly profitable firms both payables and receivables which are less trade credit. The firms which can provide the greater admission for credit of banks which can offer less trade credit for the customers. Similarly, the firms which have more bank loan have more ability to use the magic of trade credit (account receivables) by using the policy of the company.

CONCLUSION

There are different approaches can be used to manage the working capital management in financial growth cycle. Theories and empirical investigations show a clear overview about non-financial (Berger and Udell, 1998). Earlier studies focus on the trade credit which are important to manage the short term finance of firms in the shape of account receivables and account payables. So, the firms can take use of credit in two aspects; by providing the credit sale to its customers and presenting it the balance sheet as debtors in regular market as short term finance. Secondly, the firm can take the credit purchase by its suppliers by putting the accounts payables on the balance sheet in liability side. Empirical data show that over 80% of business-to-business transactions in United Kingdom are made on credit.

There are the subsequent benefits of credit: decreases of operational expenses, increases in sales, the emerging of associate rate on return and the establishing of steady commercial relations with buyers. On the request side, trade credit can be measured as short term arrears in terms of accounts owed. The benefits of trade acclaim are as follow. Firstly, trade credit was efficient approach to speech monetary frictions. Secondly, agreeing to credit limiting theory cannot admittance to the outdated financial system.

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FUTURE RECOMMENDATIONS

In Pakistan mostly firm uses trade credit for ends, credit sales and credit purchase. This study focuses different sectors of Stock Exchange but it can be analyzed by using some specific sectors to see the trade impact more specifically and its effects can be drawn according to the needs and demands of the industry. As in developing countries, the different industry have different trends and present the different from rest of the economy.

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