INTERNATIONAL JOURNAL OF INNOVATIVE RESEARCH & DEVELOPMENT

ISSN 2278 – 0211 (Online)
ISSN 2278 – 7631 (Print)

Comparative Analysis of Reported and Inflated Financial Ratio

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Abstract:
Inflation is a rise in the general level of prices of goods and services in an economy over a period of time. This study investigates the impact of inflation on companies' financial performance and financial position by evaluating and comparing reported and inflated financial ratios. Financial statements of 42 manufacturing companies covering 7 industrial sectors have been restated in current purchasing power for a period of 5 years (2004-05 to 2008-09). The ratios were calculated on both historical and adjusted financial statements to form two sets of ratios. The Current Purchasing Power method and Financial Ratio analysis have been employed to study the impact of inflation on different financial ratios. This study offered valuable information and results showed that with the impact of inflation there is significant difference in liquidity, profitability and activity ratios except quick ratio.

Key words: *Manufacturing Firms, Financial Ratios, Inflation, Statistical Analysis*

1. Introduction

Inflation refers to a continuous rise in general price level which reduces the value of money or purchasing power over a period of time. Regardless of that, the effects of inflation on the financial performance of economic units go unrecognized in published financial statements. The primary purpose of the financial statements of a company is to give a true and fair picture of financial performance (i.e. profit or loss) of the company for a particular period and financial position (assets and liabilities) of the company for a particular point of time. The impact of inflation comes in the form of rising prices and the financial statements are prepared on Historical cost basis, so they don't take into consideration of rise in the price level on different items of financial statements. This may sometimes result into the overstated profits, underpriced assets and misleading picture of Business etc. So, the financial statements presented under historical cost based accounting generally do not reflect the current worth of business. This deprives the different stakeholders like management, shareholders, and creditors etc. to have a right picture of business to make appropriate decisions.

Therefore, historical cost based accounting information about the operations of companies has ignored the effects of inflation. But the users of financial information, need relevant and reliable information about the financial position, performance and changes in the financial position of firms for making economic decisions. Inflation, on the other hand, distorts financial information by creating an impact on the firm's operational and financial results. In a hyperinflationary economy, reporting of operating results and financial position without restatement is misleading and thus is not useful. Therefore, it is necessary that financial statements reflect the true picture and are free from the negative effects of inflation.

Even though inflation accounting has long been debated, a necessary attention is avoided to provide its effects on financial statements of businesses. Hence, this study involves the impact of inflation on different financial ratios as well as a comparative study of reported and inflated financial ratios. For the purpose, 10 ratios categorized under three groups are analyzed.

2. Literature Review

Gupta Ramesh and Bhandari L C (1978), in the article "Impact of Inflation Accounting on Corporate Profits - A Study of 57 Indian Companies" mention that the whether accountants should be required to adjust reported income for inflation. The objective of this article is to measure the impact of inflation on reported profits and relevant financial ratios. The earnings of 57 companies covering 9 industries have been restated for a period of 7 years (1970-1976). The results emphasize the differential effects on companies with varying inflation rates with general price level adjustments and the significance of monetary gains and losses. The effects of restatement on dividend coverage and tax burden have been suitably highlighted. D. J. Daly (1982), in the article "Inflation, Accounting and its Effect, Canadian Manufacturing, 1966-82", provides estimates of the effects of inflation in Canada on the reported

rate of return in manufacturing firms from 1966 to 1982. It provides estimates for several different concepts of rate of return (both for all assets, whether financed by equity or debt, and for the narrower equity to the owners) and for both a narrow and wide range of financial assets. Comparisons are made with similar studies for the United Kingdom.

Shalom Hochman and Oded Palmon (1985) in the article "The Impact of inflation on the Aggregate Debt-Asset Ratio" demonstrate the impact of inflation on the aggregate debt-asset ratio cannot be determined theoretically.

However, it is shown that inflation is likely to increase this ratio when personal income tax schedules are indexed to the price level and/or when leverage-related costs are relatively high and the personal tax rate on income from holding common stocks is relatively low. Whittington G., Saporta V and Ajit Singh (1997), in their working paper "The Effects of Hyper-Inflation on Accounting Ratios Financing Corporate Growth in Industrial Economies" described the hyper-inflation can have a severe distortionary effect of the pattern of corporate finance which is apparent from company accounts. A simple algorithm, based upon the method of inflation accounting applied in Brazil, is developed and applied to the accounts of Turkish listed companies for the period 1982-90. The adjusted figures give a more plausible picture of corporate profitability and growth, and this suggests that the adjustment method is substantially successful.

Ambrish Gupta (2000), in his research entitled to "Inflation Accounting- The Indian Context", this study was a modest effort towards a systematic and comprehensive analysis of various aspects for inflation accounting and looks for offering an acceptable solution to this problem in the Indian context. It also made an assessment of the its effect of inflation on the profitability plus financial position, respectively, of the corporate entities, in addition to above it attempt to make an overall review of the financial statements, through ratio analysis and funds flow analysis, in the light of inflation. This study moreover reflects effects of inflation, over sixteen years between 1983-84 to 1998-99, on the financial health of Oil India Ltd. Karapinar A. andZaif F., (2005), in their article "Enflasyon Muhasebesinin Finansa lTablolar Analizine Etkisi, (The Effect of Inflation Accounting on Financial Statement Analysis)" In their study, Karapinar and Zaif examined the effects of inflation on accounting practice of companies' financial ratios. Their sample covered the 73 non-financial companies listed Istanbul Stock Exchange as of 2003. The ratios were calculated on both historical and adjusted numbers of financial statements to form two sets of ratios. Results showed that there was no significant change in liquidity, financial, profitability and activity ratios except fixed asset turnover ratios. Akdoğan, Aktas and Unal, in their study in 2009, extended the number of companies in the sample of Karapınar and Zaif. The results covering 146 companies were consistent with the findings of Karapınar and Zaif's study. Their results revealed that a statistically significant change for the whole sample occurs only on Total Assets Turnover. Other ratios did not show any considerable difference.

Charles N'cho-Oguee, Daniel L. Blakley, L. William Murray, and Marolee Beaumont Smith (2011), in their article "Econometric Analysis of Functional Relationship between Inflation and Growth of Firms in South Africa: Empirical Research Findings" this research is to investigate the impact inflation and other factors on the growth of business firms operating in South Africa. Data sets of South African firms' financial statements over the period of 1983-1990 were assembled to permit a detailed examination of the impact of inflation on firm's financial ratios. It has concluded that firm's debt-to-equity, sales-to-assets, and profitability ratios are all positively associated with growth and adversely affected by high inflation; a firm's working capital-to-sales ratio is negatively related to growth and is positively affected by high inflation; and there is a real, measurable impact of the financial instabilities associated with apartheid on firm's growth. Aydın Karapinar, Figen Zaifand Rıdvan Bayirli (2012), this study investigates the impact of inflation accounting application on key financial ratios. These studies related to the financial statements of 132 companies listed in the Istanbul Stock Exchange (ISE) are studied. An analysis of paired samples t test has been conducted on the financial ratios of the companies. The results showed that a significant difference between adjusted cost based financial ratios and historical cost based financial ratios occurs only for current, ratios, equity ratios and noncurrent turnover ratios. The study offered valuable information as to analyzing companies operating in hyperinflation economies. In India serious thinking on having to adjust historical cost accounts to price level change has been rather few and far between.

3. Objectives of The Study

The objectives of the proposed study are to find the impact of inflation on financial performance &position through analyzing financial ratios. The objectives of the proposed study are:

- To analyst the impact of inflation on different financial ratios of manufacturing companies in India
- To study the comparison between reported and inflated financial ratios of manufacturing companies in India.

4. Hypotheses for the Study

To study the research problems and to attain the research objectives, a hypothesis has framed. Broadly, I have attempted to test the null hypothesis against the alternative hypothesis. The null hypothesis and the alternative hypothesis framed for the purpose are:

- Null Hypothesis (H_{03}): There is no significant difference in between reported and inflated financial ratios.
- Alternative Hypothesis (H_{a3}): There is a significant difference in between reported and inflated financial ratios.

5. Methodology and Tests Used In the Study

The work conducted is a study of 42 undertakings, selected randomly from manufacturing sectors operating in India. The companies so selected are capital intensive, where there is a heavy investment in fixed assets and inventories, profitable and following the same accounting practices throughout the period of study. These sample companies belong to different sectors, viz. Auto, Cement, Chemical, Fertilizer, Food, Petroleum and Steel.

The year-end financial statements of sample companies were used for the comparing the reported and inflated performances. The published annual reports, books, journals, web pages, etc. of the selected companies form the main sources of information. The data so collected are analyzed with the help Current Purchasing Power Method (CPP), Financial Statement Analysis (FSA) and Statistical tools such as; Average, Variance Standard Deviation, Kurtosis, Skewness, and t-test are employed too to draw meaningful conclusion. The t-test is used to compare the values of the means from two groups. The two sample of t-test has been performed because the variances of two groups are assumed to be unequal.

5.1. Current Purchasing Power Method

Current Purchasing Power Method of accounting requires the companies to maintain the financial statements on conventional historical cost basis, but it further requires presentation of supplementary statements in items of current purchasing power of currency at the end of the accounting period. In this method the various items of financial statements, i.e. balance sheet and profit and loss account are adjusted with the help of recognized general price index. The consumer price index or the wholesale price index prepared by the Reserve Bank of India can be taken for conversion of historical costs. However, WPI (All Commodities) is being used in this study.

5.2. Conversion Process

For analyzing the impact inflation on reported financial performance the Historical Cost Based (HCB) accounting, financial statements for all the years from 2004-05 to 2008-09 were converted into Accounting for Current Purchasing Power (CPP) financial statements in terms of the index number prevailing in the month of March 2009. The adjustments for inflation are based on movements in wholesale price index.

Year	Average	Average as per 2004-05	Year End	Year End as per 2004-05
2000-01	83.19	100.00	84.00	100.00
2001-02	86.18	103.59	85.48	101.76
2002-03	89.12	107.13	90.60	107.86
2003-04	93.98	112.97	94.93	113.01
2004-05	100.07	120.29	100.00	119.05
2005-06	104.50	125.62	105.70	125.83
2006-07	111.40	133.91	112.80	134.29
2007-08	116.60	140.16	121.50	144.64
2008-09	126.00	151.46	123.50	147.02

Table 1: Wholesale Price Index in India [2000-09]
Source: Handbook Of Statistics On Indian Economics: RBI, 2008-09 Sept15 2009, Office of Economic Advisor Ministry of Commerce and Industry

The conversion process of Historical Cost Based (HCB) accounting financial statements for from 2004-05 to 2008-09 into Accounting for Current Purchasing Power (CPP) financial statements in terms of the index number prevailing in the month of March 2009.has elaborated below:

- All items of Profit &Loss Account, except Inventory Cost, Depreciation, Taxation, and Equity Dividend have been restated with reference to the "average price index of the year/period" as applicable to the individual year.
- Inventory cost has been restated after segregating opening balance of inventories, purchases of raw materials and closing balance of inventories as follows:
- Opening balance of inventories restated in previous year average price index.
- Closing inventories and purchases of raw materials restated in average year price index as applicable to the individual year.
- Fixed Assets and Depreciation cost of all the years of study has been adjusted to year base year 2000-01 at year end price index
- Taxation, Dividend on equity shares have been restated with reference to the "end of the year/period index" as applicable to the individual year
- The CPP Method divides the Balance Sheet items into two categories: Monetary items and Non-monetary items. Monetary items are those assets and liabilities the amounts of which are fixed by contract or statute in terms of the number of rupees irrespective of the changes in the purchasing power of rupee. Items which comes under monetary in nature are as follows:
- Monetary assets include Investments, which are fixed in rupees, Current Assets other than Inventories.
- Monetary Liabilities include Secured Loans, Unsecured Loans, Current Liabilities and Provisions

Since the value of monetary items is fixed in rupees, they are already expressed in terms of current purchasing power of rupee and, therefore, need no restatement. For Calculating purchasing power gain/loss, the balance of net monetary liabilities/assets as on the date of the Balance Sheet is bifurcated into opening balance and additions/decrements thereto during the year. The opening balance is restated with reference to the index prevalent on that date. Additions/decrements are restated with reference to the average index of the year. The closing balance is deducted from the total of restated opening balance and additions/decrements. The resultant figure, if positive, is gain otherwise loss in the case of net monetary liabilities and vice versa in the case of net monetary assets.
After converting the Historical Cost Based (HCB) financial statements into Current Purchasing Power (CPP), the financial ratios have been calculated. The calculated ratios are presented in Table-2.

Liquidly Ratios	**Profitability Ratio**
Current Ratio	Gross Profit Margin
Quick Ratio	Operating Profit Margin
Activity Turnover Ratio	Net Profit Margin
Debtor Turnover Ratio	Return on Investment
Creditor Turnover Ratio	Dividend Payout Ratio
Inventory Turnover Ratio	

Table 2: Ratios Used In the Study

6. Comparative Analysis of Reported and Inflated Liquidity Ratios
These ratios are calculated to comment upon the short-term paying capacity of a firm or a concern's ability to meet its current obligation. The important liquidity ratios are current ratio and quick ratio. The Table -3 shows the Liquidity Ratios (current ratio and quick ratio) of sample companies from the year 2004-05 to 2008-09 under both the methods: HCB and CPP Method.

Year	**Current Ratio**		**Quick Ratio**	
	HCB Method	**CPP Method**	**HCB Method**	**CPP Method**
2004-05	1.26	1.32	1.03	1.03
2005-06	1.31	1.35	1.05	1.05
2006-07	1.36	1.39	1.13	1.13
2007-08	1.63	1.64	1.33	1.33
2008-09	1.31	1.31	1.10	1.10

Table 3: Liquidity Ratios

6.1. Current Ratio
Current ratio is a measure of general liquidity and is used to make the analysis of a short-term financial position or liquidity of an organization. It represents the margin of safety. It is the relationship between the current assets and current liabilities. The relationship has been computed by dividing current assets with the current liabilities. A review on the above Table reveals that current ratio of sample companies has shown an increasing trend in the entire study period except the last year i.e., 2008-09. The absolute value of this ratio was 1.26 in 2004-05, which increased to 1.63 in 2007-08; but then declined to 1.31 in 2008-09 under HCB Method. Under the CPP Method, the ratio has also shown the similar trend, it gone up from 1.32 in 2004-05 to 1.64 in 2007-08 and then came down to 1.31 in the last year. Hence, the current ratios of sample companies are higher in case of CPP Method as compared to HCB Method in all the years except for the last year (2008-09), when the ratio stood one and the same, (1.31:1) under both the methods. However, the improvement of current ratio under CPP Method is very nominal, because inflation has affected non-monetary current assets and non-monetary current liabilities in the same proportion. Only the inventory holding has registered a higher growth than the inflation level. Hence it recorded an expansion under CPP Method.

6.2. Quick Ratio
Quick ratio is also known as Acid Test Ratio or Liquid Ratio. It is a fairly stringent measure of liquidity. It is based on those current assets, which are highly liquid. It is the relationship between the quick assets and current liabilities. It has been calculated by dividing quick assets by the current liabilities. Inventories are excluded from the current assets to find out quick assets. Table-3 reveals that quick ratios of sample companies remains unchanged under both the methods, HCB and CPP; for all the year of study i.e.; from 2004-05 to 2008-09. It is because of the fact that, the inflation has affected non-monetary current assets and non-monetary current liabilities in the same proportion as the inventories have been excluded from current assets to get quick assets.

7. Comparative Analysis of Reported and Inflated Profitability Ratios

This group of ratios measures the overall performance and effectiveness of the firm. The main profitability ratios include Gross Profit Margin, Operating Profit Margin, Net Profit Margin, Return on Investment and Dividend Payout Ratio etc. The Table-4 shows the results profitability ratios under HCB method and CPP method form 2004-05 to 2008-09.

Year	Gross Profit Margin (%)		Operating Profit Margin (%)		Net Profit Margin (%)		Return on Investment (%)		Dividend Payout Ratio (%)	
	HCB	CPP	HCB	CPP	HCB	CPP	HCB	CPP	HCB	CPP
2004-05	29.18	28.74	18.47	17.23	11.24	8.28	52.89	44.26	36.60	60.78
2005-06	22.99	22.64	15.62	14.36	9.80	7.61	45.16	36.31	37.54	54.63
2006-07	23.51	22.97	15.42	13.90	10.35	8.69	46.18	35.43	32.68	55.47
2007-08	23.60	23.25	15.24	13.62	9.61	8.62	38.49	29.56	32.24	70.47
2008-09	22.87	22.23	13.67	11.53	8.29	6.45	48.58	31.23	31.15	47.13

Table 4: Profitability Ratios

7.1. Gross Profit Margin

Gross profit margin measures the relationship of gross profit with sales and indicates the margin left after meeting manufacturing costs. It is clear from the Table-4 that the gross profit margin of sample companies for both the method i.e. HCB and CPP is fluctuating over the five years of study from 2004-05 to 2008-09. It recorded a high of 29.18 percent and 28.74 percent in 2004-05 and a low of 22.87 percent and 22.23 percent in 2008-09 under HCB Method and CPP Method respectively. During the entire period of study, the Gross profit margin under HCB Method has witnessed slightly higher trend as compared to CPP Method. Consequently the inflation has brought down the production efficiency of the sample companies.

7.2. Operating Profit Margin

Operating Profit Margin shows the relationship between operating profit and sales. The above Table it evident that under HCB method, the operating profit margin of sample companies showed a declining trend in the period of study. The value of this ratio was 18.47 percent in 2004-05 and reduced to 13.67 percent in the last year of study. Similarly, under the CPP method the ratio has gone down from 17.23 percent to 11.53 percent over the same period. Furthermore, it is apparent from the Table that volume of Operating Profit Margin is higher in HCB Method in all the years under study as compared to CPP Method without any exception. It gives good reason to conclude that inflation has dwindled for the operating efficiency of the sample companies.

7.3. Net Profit Margin

Net Profit Margin establishes a relationship between Net Profit (Profit after Tax) and Sales and indicates the overall efficiency of the management in manufacturing, selling, administrative and other activities of the organization. The Table-4 points out that net profit margin of sample companies has fallen down from 11.24 percent in 2004-05 to 8.29 percent in 2008-09 under HCB method, whereas in case of CPP method it dropped from 8.28 percent to 6.45 percent during same period. It can also be observed that in all the years of study there is a wide gap in net profit margin between the HCB method and CPP method. The variation between two net profit margins (HCB and CPP) was highest (2.96 percent) in the year 2004-05 and lowest (0.99 percent) in the year 2007-08. Thus the inflation has badly hit the overall profitability position of the sample companies during the period of study.

7.4. Return on Investment

Return on Investment (ROI) is one of the most important ratios used for measuring the overall efficiency of the organization, as the objective of organization is to maximize its earnings. From the Table it is apparent that ROI has a declining trend in HCB method during the study period except the last year 2008-09. The value of this ratio varies between 52.89 percent (2004-05) and 38.49 percent (2007-08). Similarly, ROI under CPP method has a declining trend in all the years of study except the year 2008-09. The absolute figures of this ratio decreased from 44.26 percent to 31.23 percent over the span of five years i.e. from 2004-05 to 2008-09 after recorded a low of 29.56 percent in 2007-08. While comparing the two accounting methods, it is clear that ROI is much higher in case HCB, than CPP in all the years under study without any exception. The discrepancy between two methods (HCB and CPP) is highest (17.35 percent) in the year 2008-09 and lowest (8.63 percent) in the year 2004-05. Thus it can be concluded that ROI of the sample companies has been badly affected by inflation during period under our study.

7.5. Dividend-Payout Ratio

It is the percentage of earnings paid to shareholders in dividends and provides an idea of how well earnings support the dividend payments. More mature companies tend to have a higher payout ratio. It is observed from the Table-4 that the dividend payout ratio in HCB Method has gone down from 36.60 percent to 31.15 percent during the study period i.e. 2004-05 to 2008-09. But in the case of CPP method the dividend payout ratio fluctuated in between 70.47 percent (highest) and 47.13 percent (lowest) during the period of study. Table-4 also reveals that HCB dividend payout ratio is lower than CPP dividend payout ratio throughout the period of study to a

large extent. It means the sample companies have kept less profit and distributed more to the shareholders as dividend. It definitely affects the net worth of the sample companies.

8. Comparative Analysis of Reported and Inflated Activity Ratios

Activity ratios are calculated to measure the efficiency with which the resources of a firm have been employed. These ratios are also called turnover ratios because they indicate the speed at which the assets are being turned over into sales.

Year	Creditor Turnover Ratio		Debtor Turnover Ratio		Inventory Turnover Ratio	
	HCB Method	CPP Method	HCB Method	CPP Method	HCB Method	CPP Method
2004-05	3.40	4.23	21.57	26.61	12.51	12.18
2005-06	3.77	4.50	21.79	25.75	11.44	11.22
2006-07	3.85	4.34	24.08	26.69	12.12	11.74
2007-08	3.76	4.06	23.97	25.39	11.89	11.65
2008-09	3.90	3.93	26.40	25.87	13.97	13.37

Table 5: Activity Ratios

The Table-5 elaborates the activity ratios; viz. Debtor Turnover Ratio, Creditor Turnover Ratio and Inventory Turnover Ratio of sample companies of both under HCB Method as well as CPP Method for the study period i.e. from 2004-05 to 2008-09. The trend of these ratios has discussed in the subsequent paragraphs.

8.1. Creditors Turnover Ratio

In the course of business operations, an organisation has to make credits purchases and incur short-term liabilities. A supplier of goods i.e., creditors are naturally interested in finding out how much time the organisation is likely to take to repay its trade creditors. Higher creditor turnover ratio is good because it decreases the average payment period. It depicted from the Table that, HCB creditor turnover ratio of sample companies has increased from 3.40 times to 3.90 times during 2004-05 to 2008-09, whereas CPP creditor turnover ratio has turned down from 4.23 times to 3.93 times over the years after recording a high of 4.50 times in 2005-06. Over again while comparing this ratio under both the methods; it is revealed that CPP creditors' turnover ratios are higher than that of HCB for all the years except the year 2008-09. It indicates that the suppliers have been treated in a better manner under CPP method as compared to HCB method.

8.2. Debtor Turnover Ratio

Debtor turnover ratio indicates the velocity of debt-collection of an organization. In simple words, it indicates the number of times debtors (receivables) are turned over during a year. Generally a high turnover ratio is an indicator of efficiency in management of debtors to sales. By looking into the Table, it can observed that in case of HCB method the debtor turnover of sample companies has improved over the study period where as in case of CPP method it was worse during the period. The debtor turnover ratio found 21.57, 21.79, 24.08, 23.97 and 26.40 times from 2004-05 to 2008-09 respectively in HCB method but, in the case of CPP method it is 26.61, 25.75, 26.69, 25.39 and 25.87 times correspondingly over the study period. Moreover by comparison, it is found that HCB debtor turnover ratios are smaller as compared to that of CPP for all the years of study i.e. 2004-05 to 2008-09. That means the inflation has improved the efficiency in debtors management of sample companies during the period of our study.

8.3. Inventory Turnover Ratio

An Organization has to maintain a minimum level of inventory so as to be able to meet requirements of the business, but the level of inventory should neither too high nor too low. High inventory levels are unhealthy because they represent an investment with a rate of return of zero. It also opens the company up to trouble should prices begin to fall. By looking at the Table the inventory turnover ratio of sample companies in case of HCB method has varied over the study period from 2004-05 to 2008-09 after recording a high of 13.97 times in 2008-09 and low of 11.44 times in 2005-06. But in case of CPP inventory turnover ratio has come down from 12.18 times during 2004-05 to 11.22 times during 2005-06 and finally it reached to 13.37 times in 2008-09. In the assessment of HCB inventory turnover ratio and CPP inventory ratio, it is clearly observed that inventory turnover ratios are higher in the case of HCB method as compared to CPP method for all the years of study i.e. from 2004-05 to 2008-09. So it concluded that inventory turnover ratio of sample companies has suffered in the inflationary condition

9. Testing Of Hypothesis

For testing whether there a significance difference between reported and inflated financial ratios exist or not, t-test has been employed between the reported and inflated financial ratios.

Particulars	t- Statistics	p-Value
Current Ratio	-2.1502	0.0188
Gross Profit Margin	2.9901	0.0024
Operating Profit Margin	3.7177	0.0003
Net Profit Margin	5.1103	0.0000
Return on Investment	3.4662	0.0006
Creditor Turnover Ratio	-7.5652	0.0000
Debtor Turnover Ratio	-6.0256	0.0000
Inventory Turnover Ratio	5.5831	0.0000

Table 6

The table-6 indicates t-Statistics and p-Value of the t-test between the reported and inflated financial ratios. It can find out from the table that all the ratios' p-value found to be less than 0.05, which indicates a significant difference in the value of financial ratios between the two accounting methods at 5 percent level of significance. Hence our Null Hypothesis (H_{01}- There is no significant difference in between reported and inflated financial ratios) is rejected as there is a significance difference in reported and inflated financial ratios. Therefore the Alternative Hypothesis (H_{a1}) is accepted.

10. Conclusion

From the above analysis and comparisons of reported and inflated financial ratios, certainly it has detected that inflation has affected all the ratios under study except the quick ratio. Under inflationary condition the current ratio, creditor turnover ratio and debtor turnover ratio have changed between two accounting method and performed better, but no change has transpired to the quick ratio. On the other hand all the profitability ratios and inventory turnover ratio have suffered due to inflation. Moreover, the dismal performance revealed under the CPP method points towards the efficiency of the management in fighting against inflation. Whatever view one takes, no one can deny that, but inflation has taken its toll. The performance which otherwise appears to be quite good, turned out to be very dismal, when adjustments for current purchasing power of rupee are made. The CPP method adjustments have thus proved that historical profitability is a fairy story. The financial ratio analysis thus confirms the findings that historical accounts overstate financial performance and understate financial position.

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