

-RESEARCH ARTICLE-

## INVENTORY TURNOVER, ACCOUNTS RECEIVABLE TURNOVER, AND MANUFACTURING PROFITABILITY: AN EMPIRICAL STUDY

### Ruaa Binsaddig

Department of Finance, College of Business  
Administration, University of Business and  
Technology, Jeddah, Saudi Arabia  
Email: [r.binsaddig@ubt.edu.sa](mailto:r.binsaddig@ubt.edu.sa)  
<https://orcid.org/0000-0002-8436-7218>

### Anis Ali

Department of Management, College of Business  
Administration, Prince Sattam Bin Abdulaziz  
University, Al kharj 11942, Saudi Arabia  
Email: [ah.ali@psau.edu.sa](mailto:ah.ali@psau.edu.sa)  
<https://orcid.org/0000-0001-7799-6043>

### Talal Al Alkawi

Accounting and Finance Department,  
Applied Science University, Kingdom of Bahrain.  
Email: [talal.alalkawi@asu.edu.bh](mailto:talal.alalkawi@asu.edu.bh), [drtalal60@gmail.com](mailto:drtalal60@gmail.com).  
<https://orcid.org/0000-0002-0842-8234>

### Basel J. A. Ali

Accounting and Finance Department,  
Applied Science University, Kingdom of Bahrain.  
Email: [basel.ali@asu.edu.bh](mailto:basel.ali@asu.edu.bh), [basil8011@gmail.com](mailto:basil8011@gmail.com).  
<https://orcid.org/0000-0001-6259-2062>

### —Abstract—

Profitability is a criterion for determining the health of a business, so we need an analytical tool to evaluate it. The company will profit more if its inventory and accounts

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receivable turnover rates increase. Prior research identified discrepancies between inventories, receivables, and total asset turnover, as well as profitability measurements such as gross profit margin (GPM) and net profit margin (NPM), as well as ROA and ROE. This research aims to examine the link between inventory turnover (IT), accounts receivable turnover (ART), and profitability for manufacturing firms listed on the Bahrain Stock Exchange from 2012 to 2021. This research fills a gap in the literature. For empirical estimation, regression analysis has been used. The results reveal a statistically significant relationship between (IT), (ART), and profitability indices: gross profit margin (GPM). The study reveals that inventory turnover (IT) and accounts receivable turnover (ART) are crucial in predicting the profitability of a business.

**Keywords:** Accounts Receivable Turnover, Inventory Turnover, Profitability, Manufacturing sector, Bahrain.

## 1. BACKGROUND OF THE STUDY

Manufacturing businesses expand yearly due to increased competition in all industrial sectors. To optimize earnings, manufacturing businesses conclude the manufacturing process by acquiring raw materials and converting them into finished goods (Wajo, 2021). The corporation's principal objective is to maximize profits. Profitability is one of the pillars for determining the health of a company; to evaluate it, we need an analytical tool. Hence, every corporate entity wants to increase its profitability; the more profitable a company entity is, the greater its likelihood of survival. Maximum profitability must be achieved (Wang et al., 2021). Many aspects directly or indirectly influence a company's performance and decide its profitability (B. J. Ali & Oudat, 2021a; Saleh et al., 2023). These elements, which include the interest rate, the cost of products sold, the tax rate, and the quantity of inventory, often substantially impact profitability (Harban et al., 2021).

The profitability of a business may be determined using a variety of financial metrics. Investors analyze corporate financial performance when selecting whether or not to invest in a company, and it is one approach for measuring a firm's health (Saleh, 2020). The purpose of evaluating a company's performance is to determine its level of profitability (B. J. Ali & Oudat, 2021b; Harban et al., 2021; Jawabreh et al., 2021; Nawaiseh et al., 2021). The worth of a corporation will increase as its financial performance improves. Thus, business management must evaluate the firm's performance to determine if it is in good or poor health (B. J. Ali & Oudat, 2021b; Jawabreh et al., 2022; Thuneibat et al., 2022). Analysis can be accomplished by examining the financial statement to predict the financial status of the business, which will serve as the foundation for assessing the current and historical performance of the company. When the results of a company's appraisal of its financial status are

favorable, it implies its significant objectives have been met (Rajagukguk & Siagian, 2021).

Significant profits can be a benchmark for businesses seeking to remain solvent and have bright prospects. Yet, it is also essential for businesses to focus on internal business operations, such as inventory and receivables turnover rates. The company's financial statements may generate a number of financial ratios that management can use to determine if the company is experiencing poor or favorable economic conditions. Financial statements are the basis for evaluating a company's success (B. Ali, 2022; Moridipour & Mousavi, 2014; Shibly et al., 2021; Wang et al., 2021). Profitability ratios are commonly employed to evaluate a company's financial performance. The profitability ratio demonstrates a company's ability to generate a specified profit from its assets and capital (Fitria & Suartini, 2021; Harban et al., 2021). The inventory turnover rate, which should be high for a corporation to generate a profit, reveals the company's financial health. Inventory turnover ratios and profitability ratios are two ratios that can be used to evaluate an organization's health. The inventory turnover ratio measures the rate at which old inventory is replaced with new inventory once it leaves the warehouse. Businesses seeking to increase profits must also examine the accounts receivable turnover ratio. The "accounts receivable turnover" ratio evaluates how long it takes to collect an organization's receivables within a specified period (Rajagukguk & Siagian, 2021).

Raising inventory sales (IT) is a common strategy businesses use to boost profitability. Because inventory is a significant current asset, it is one of the most significant asset postings (Alrabei et al., 2022; Jawabreh et al., 2022; Manullang et al., 2020). In trade organizations, these inventories consist of commodities, whereas industrial enterprises may hold raw materials, work-in-progress, or finished goods. Inventory scarcity or excess is a negative sign. The more significant the amount of information technology (IT), the more enormous the potential for cost reductions and the greater the company's profitability (Abbas, 2017; Harban et al., 2021). the lesser the profit advantage, the slower the rate of return (IT). Getting a high-level degree in (IT) is more complex than one might expect; the firm must consider numerous operational concerns. They include regular and effective inventory management, product quality enhancement, and consumer request fulfillment (Lismana et al., 2021). Managing inventories incurs opportunity costs, carrying costs, and other expenses. Thus, it is essential to determine whether inventory control regularly affects profitability and whether efficient inventory management is advantageous (Irman & Purwati, 2020).

In light of these considerations, the primary objective of the current study/research is to examine the relationship between (IT), (ART), and profitability in manufacturing sector companies listed on the Bahrain Stock Exchange from 2012-2021. Numerous earlier studies, such as the one conducted by Suminar (2015), have asserted that IT and ART substantially boost profitability. According to Andre et al.'s (2017) findings, cash,

inventory, and accounts receivable turnovers considerably increase profitability (Rajagukguk & Siagian, 2021). Several studies have investigated the relationship between activity ratios, especially turnover ratios ((IT), accounts receivable turnover, and profitability, an issue faced by all businesses (even those in the manufacturing industry), but no evident result has been obtained. Past research has demonstrated that the outcomes may be more consistent; therefore, this field requires further investigation. This work contributes significantly to the body of knowledge in two ways: First, most studies concentrated on RON and ROE, with few studies focusing on (GPM) and little primary research on the manufacturing industry. This study examines the relationship between manufacturing industry activity ratios ((IT), (ART), and GPM. Second, and most crucially, the study focuses on the abovementioned nexus in Bahrain's manufacturing economy. According to the author's knowledge, no previous research has quantified the association between ((IT), (ART), and GPM in Bahrain's industrial industry. Bahrain's economy is expanding, and this growth is generally influenced by factors such as the performance of all listed companies and other economic organizations (Sarea & Alansari, 2016).

The manufacturing industry of Bahrain, the second largest sector (after the services sector) in terms of its contribution to the country's gross domestic product (34,3 percent), is an important area of study. Bahrain's manufacturing sector is booming and vital to the country's economy. Due to the use of contemporary and sophisticated manufacturing facilities and current trends in manufacturing performance measurement, Bahrain's manufacturing sector is considered a significant area of study (Mahmoud, 2014). In addition, past research has shown contradictory findings about the impact of various activity ratios, such as inventory and accounts receivable, on profitability measures such as (GPM), (NPMs), ROE, and ROA; thus, this topic requires further investigation. This study's findings will help Bahrain's government and officials boost the profitability of the country's most important industrial sector. Hence, the study contributes significantly to company revenues and profitability literature.

## 2. LITERATURE REVIEW

In this section of the practical study, the critical challenges in characterizing the relationship between specified turnover ratios of activity ratios and selected GPM and NPM will be discussed. This section will cover the objective appraisal of literature and the investigation of such perspectives and theories. (IT), (ART), and the turnover of total assets affect profitability ratios. Warrad et al. (2015) validated the impact of turnover rates on the performance of Jordan's service industry. According to the findings, the effect of turnover percentages on the profitability of Jordanian service enterprises was insignificant. In addition, it was noted that working capital turnover did not substantially impact the performance of the Jordanian service sector. Warrad et al. (2015) determined the impact of fixed and total asset turnover on ROA and ROE in the service sector. Multiple linear regression analysis was utilized to examine the data.

According to the investigation findings, asset turnover had a small effect on ROE. The turnover of total assets affected the ROA. [Arilyn \(2016\)](#) evaluated the impact of (IT), the average collection period, the turnover of total assets, the current ratio, and the turnover of fixed assets on profitability. IT and total asset turnover were shown to have minimal impact on profitability. [Sunjoko et al. \(2016\)](#) evaluated the effect of information technology, total assets, and the current ratio on profitability. The study's findings indicate that the current ratio and fixed asset turnover affected profitability. [Sunjoko et al. \(2018\)](#) examined the impact of total asset turnover and current ratio on bank stock returns. Using Multiple Linear Regression, the data were evaluated. According to the study's findings, total asset turnover considerably affects ROE. The asset turnover affected the return on equity. [Anwar \(2018\)](#) also investigated the impact of inventory and cash turnover on the profitability of companies listed on the Indonesian stock exchange between 2011 and 2015. Multiple linear regression determined that cash turnover had a substantial beneficial effect. In contrast, inventory turnover did not affect the profitability of the companies investigated. [Moridipour et al. \(2014\)](#) found a substantial negative correlation between (GPM) and revenue (IT).

[Amanda \(2019\)](#) investigates further the relationship between debt-to-equity ratio, cash turnover, current ratio, receivable turnover, and profitability. From 2013 to 2017, the essential chemical industry on the Indonesia Stock Exchange served as the study's sample. The research population, sampled according to predetermined parameters, is the chemical composition of the ID financial report. It was discovered that the debt-to-equity ratio, cash turnover, and receivable turnover did not affect profitability. In contrast, the current ratio had a significant and beneficial effect on profitability, as determined by regression analysis of the data. In a similar study, [Farooq \(2019\)](#) evaluated the impact of (IT) on corporate profitability. According to the study's conclusions, (ITR) did not affect the return on assets. In the second model, the internal rate of return does not affect the return on equity. The (ITR) does not influence the net profit margin ratio in the third regression model. According to the report, managers should examine the fundamental characteristics while determining the profitability of their organizations. Similar research was undertaken by [Amanda \(2019\)](#) on the effect of receivable turnover, cash turnover, and (IT) on profitability. Using step regression to analyze the data, it was determined that Cash Turnover, Receivables Turnover, and Information Technology (IT) did not affect profitability.

Between 2014 and 2018, [Fitria et al. \(2021\)](#) investigated the impact of turnover and (IT) on the profitability of automotive sector firms as assessed by the return on assets, either simultaneously or separately. According to the data, cash turnover had a marginally positive but negligible effect on profitability. The influence of turnover on profitability was generally positive and negligible, while the effect of (IT) was both positive and negative. [Wajo \(2021\)](#) evaluated the impact of inventory, cash, and accounts receivable turnover on the profitability of 16 of 137 industrial enterprises listed on the Indonesian stock exchange. The study included the years 2013 through

2016. According to the research findings, cash and accounts receivable turnovers had a considerable and favorable impact on the profitability of the listed firms. [Lismana et al. \(2021\)](#) evaluated whether cash turnover, (ART), and (IT) influence ROA by applying documentation as a data collection technique and multiple linear regression techniques with SPSS software. According to the study, cash turnover, (ART), and (IT) have little effect on ROA as a result of a drop in output, cash flow limitations owing to low (ART), and bad sales, which result in delayed (IT) and higher inventory costs. In continuation, [Indriaty's \(2021\)](#) research [Indriaty et al. \(2022\)](#) analyzed the effect of (IT), cash turnover, and receivable turnover on profitability. Throughout the first four quarters of 2020, financial records from publicly traded telecom companies were used to collect data. According to the data, information technology (IT) and accounts receivable turnover had no discernible effect on profitability.

[Herison et al. \(2022\)](#) investigated how the turnover of working capital, receivables, and willingness affected the profitability of the trading sector of the Indonesian stock market. The results indicate that operational capital had a significant and unfavorable effect. In contrast, account receivable turnover has a considerable and favorable impact on the profitability of trading sub-sectors on the Indonesian stock exchange. [Rajagukguk et al. \(2021\)](#) investigated the effects of inventory and account receivable turnover on profitability and discovered that both variables had a positive and statistically significant effect on profitability. [Eryatna et al. \(2021\)](#) also analyzed the impact of cash turnover, inventory turnover, and accounts receivable turnover on the profitability of 51 consumer product-producing countries listed on the Indonesian stock exchange from 2016 to 2018. Using a multiple linear regression model, the study found that cash turnover did not impact company profitability. However, inventory and account receivable turnover had a significant and favorable impact. [Kartika et al. \(2023\)](#) also investigated the relationship between inventory turnover and accounts receivable turnover on the profitability of food and beverage partnerships. The authors determined that both variables contributed positively to profitability.

## 2.1 Research Gap

Previous studies concluded that IT significantly and positively affects profitability ([Fitria & Suartini, 2021](#); [Moridipour & Mousavi, 2014](#); [Qazi et al., 2011](#)). While studies such as ([Amanda \(2019\)](#), [Indriaty \(2021\)](#), [Lismana et al. \(2021\)](#), and [Manullang et al. \(2020\)](#)) determined that ART does not affect profitability, [Amanda \(2019\)](#), [Indriaty \(2021\)](#), [Lismana et al. \(2021\)](#), and ([Manullang et al. 2020](#); [However et al., 2017](#)) found that (ART) has a significant negative impact on profitability. Based on these results, it is acceptable to conclude that past investigations have yielded disparate conclusions, which motivates the researcher to investigate the nexus further. However, according to the author's best knowledge, none of the available research has quantified the relationship between IT, ART, and GPM in Bahraini manufacturing enterprises. The varied findings imply a theoretical research gap, while the lack of research in the

setting of Bahrain implies a research need in the context. After identifying these gaps, the objective of this study is to assess the relationship between the activity ratios (IT), (ART), and (GPM) in Bahrain from 2012 to 2021.

## 2.2 Hypotheses

According to the findings of previous studies, earlier investigations have uncovered a correlation between activity and profitability ratios. Consequently, the following hypotheses can be formulated:

HA<sub>1</sub>: The inventory turnover ratio significantly correlates with the gross profit margin.

HA<sub>2</sub>: The accounts receivable turnover significantly correlates with the gross profit margin.

## 3. RESEARCH METHODOLOGY

### 3.1 Sample Design

This quantitative study examines the relationship between GPM, the dependent variable, and the turnover rates of inventory and accounts receivable, the independent variables. The study focuses specifically on the relationship between these three characteristics. The population of this study consisted of all manufacturing enterprises registered on the Bahrain stock exchange between 2012 and 2021. The scope of the investigation was from 2012 to 2021. Four of these companies represented the entirety of the companies listed on the Bahrain stock exchange. The manufacturing sector in Bahrain is developing, and the study sample is representative of its most significant contributions to Bahrain's gross domestic product (34.4%). All of the accounting data used in this study was obtained from the annual reports and annual bulletins provided by the Bahrain bourse while examining these businesses. This information was obtained from the website of the Bahrain bourse.

The study models:

$$GPM = \beta_1 + \beta_2 ITR + \beta_3 ARTR + \varepsilon$$

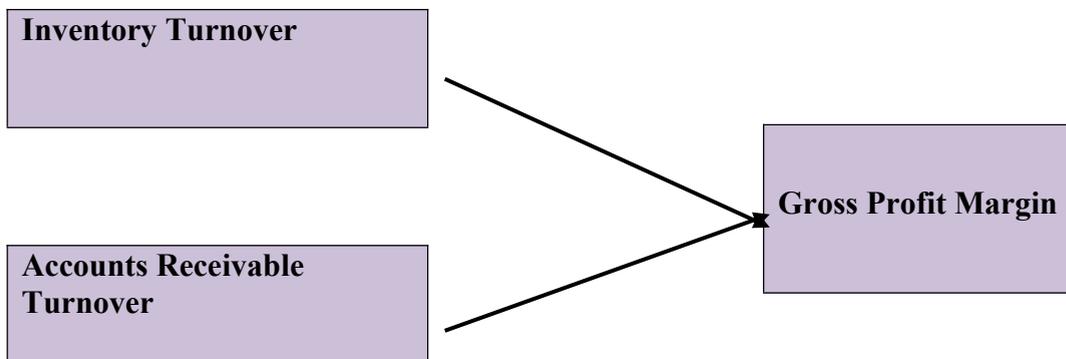
**Table 1. Measurement of Variables**

Variables	Measurement of variables	Cited by
(IT)	COGS / ((beg. inv. + End. Inv.)/2)	(Abbas, 2017)
(ART)	Net Annual Credit Sales ÷ Average Accounts Receivables	(Manullang et al., 2020)
GPM	Gross Profit / Net sales	(Mappanyuki & Sari, 2017)

#### 4. CONCEPTUAL FRAMEWORK

Using a conceptual framework, this study aims to examine the relationship between activity ratios and profitability ratios in Bahrain. This evaluation will be carried out in Bahrain. Figure 1 provides a graphical depiction of the framework.

Figure 1: Conceptual Framework



#### 5. ANALYSIS AND INTERPRETATION

The purpose of analyzing the data from the research was to draw conclusions and give recommendations. This analysis was carried out using statistical software tools (SPSS).

##### 5.1 Descriptive Statistics of Variables

The results of different descriptive statistics on variables are summarized in table 2, which can be viewed below.

Table 2: Variables' Descriptive Statistics

Variables	Obs.	Minim	Max	Mean	S, Deviation
(ART)	40	1.827	6.556	4.10820	1.369773
(IT)	40	.543	2.013	1.21360	.497074
(GPM)	40	-1.557	.297	-.20618	.646280

According to Table (3), the shortest (ART) times in the sampled industrial sector were 1.827%, while the most extended times were (6.556). The mean was 4.108, and the standard deviation was 1.36, indicating that the manufacturing sector of the Bahrain market is exhibiting positive trends. The sampled manufacturing industry had the lowest (IT) of (.543), while the manufacturing industry with the highest (IT) was (2.013). The mean indicated (1.213) times, and the standard deviation was (0.497) times, indicating encouraging indicators for the Bahrain Stock Exchange manufacturing sector.

## 5.2 Multicollinearity Test

According to Table 3, the tolerance calculation reveals that no independent variables have tolerance values of less than 10 percent. All tolerance values exceed 10%, indicating no correlation between the variables. Calculating the variation inflation factor (VIF) resulted in the same conclusion. There are no independent variables with a VIF value exceeding 10, and all VIF values are less than ten. The tolerance value test concludes that activity and GPM are not multicollinear. This observation confirms the hypothesis.

**Table 3: Summary of Multicollinearity Tests**

Model	Collinearity Statistics	
	Tolerance	VIF
(IT)	.664	1.505
(ART)	.664	1.505
a. Dependent Variable: Gross Profit Margin		

## 6. PEARSON CORRELATION TESTING

Using the Pearson Correlation Technique, the interdependence of the variables was examined to evaluate whether or not the relationship could cause problems. The research variables' Pearson correlation coefficients are presented in Table 4, which may be found below. According to, the correlation parameters are less than 0.07. (Hair et al., 2017). When the correlation between the various study variables approaches 0.07, there is no cause for alarm. It is trivial to determine the regression coefficients using the variable correlation.

**Table 4. Correlations**

	(IT)	(ART)	(GPM)
(IT)	1		
(ART)	.579**	1	
(GPM)	.650**	.854**	1

Table 5 displays an R2 value (R Square) of 0.875, corresponding to an 87.5% impact of independent variables. It indicates that the independent variable, which consists of (IT) and (ART), has an 87.5 percent influence on the dependent variable (GPM). The non-research variable influences the profitability of manufacturing enterprises listed on the Bahrain stock exchange by 12.5%.

**Table 5: Results Coefficient of Determination Regression Model GPM**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson

1	.875 <sup>a</sup>	.765	.752	.321556	.782
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## 7. REGRESSION ANALYSIS

In the research, we worked with three different regression variables: IT, ART, and GMP. These are the variables of the model.

**Table 6. Regression Model**

Model			Beta	t	Sig.
	B	Std. Error			
(IT)	.304	.127	.234	2.390	.022
(ART)	.339	.046	.718	7.349	.000

## 8. RESULTS OF ANALYSIS

The following set of hypotheses is evaluated with the use of regression analysis to assess whether or not they have been confirmed:

**HA<sub>1</sub>: The inventory turnover ratio significantly correlates with the gross profit margin.**

The results of testing hypothesis 1 are displayed in [table 6](#), where it can be seen that the ratio of the independent variable (IT) positively affects GPM, as indicated by its significance level of 0.022. The H1 hypothesis of a significant association between IT and GPM is supported by the t-statistic value (2,390.00) and the P-value (.022). The fact that the (IT) significance level is less than 0.05 supports the possibility that H1 can be accepted. Hence, the (ITR) favorably impacts GPM in the Bahrain Manufacturing sector listed on the Bahrain stock exchange. This is consistent with the pecking order hypothesis since enterprises still have adequate internal capital resources, such as retained earnings. As previously stated, the results of the current study are consistent with those of ([Dewi, 2014](#); [Fitria & Suartini, 2021](#); [Lestari & Farida, 2017](#); [Mwaura, 2017](#); [Wajo, 2021](#)).

**HA<sub>2</sub>: The accounts receivable turnover significantly correlates with the gross profit margin.**

The results of the correlation between (ART) and (GPM) are shown in [Table \(6\)](#) with a (t. statistic) value of (7,349) and a P-value of (0.000), indicating a statistically significant relationship between (ART) and (GPM) (GPM). These results directly validate the second hypothesis regarding activity ratios with (GPM) for the Bahrain Manufacturing sector contained in the Bahrain market listing. Also, it signifies that the company's profitability chances are improving. This is consistent with the pecking order concept, which favors utilizing internal funding sources, given that enterprises still have sufficient internal sources of capital, such as retained earnings. This is due to

the company's capacity to collect receivables promptly and efficiently, convert them into cash, and use that cash to operate its business profitably (Herison et al., 2022). This study gives credibility to the results of (Abbas, 2017; Herison et al., 2022; Rajagukguk & Siagian, 2021; Wajo, 2021).

## 9. CONCLUSIONS AND RECOMMENDATIONS

The purpose of this study is to evaluate the relationship between the activity ratios (IT), (ART), and profitability ratios (GPM) of the manufacturing sector of the Bahrain Stock Exchange from 2000 to 2008. (2012-2021). For this aim, descriptive statistics analysis, multicollinearity testing, Pearson correlation testing, and regression studies have been conducted. The findings reveal a substantial relationship between (IT), (ART), and GPM. It may be determined from the research and discussion that the operation will be more profitable, as represented by the gross profit margin, the higher the turnover ratios. When the amount of accounts receivable is more significant, the company's assets are turned over more quickly and efficiently, indicating a higher likelihood of profitability. As the inventory turnover rate rises, maintenance expenses fall. More profitability correlates to decreased expenses for the business.

The outcomes of this study suggest that companies should pay greater attention to ITR and ATR to optimize profits and improve financial performance more effectively and efficiently. Before investing funds, investors should evaluate a company's performance to forecast future profits (profits made each year). Factors influencing profitability, such as sales and investments or fixed asset turnover, should be addressed. Based on the relevance of inventory and account receivable turnover, the study's conclusions can aid investors in estimating or predicting the possible rate of return on investments. To maximize earnings, a business may consider these variables while formulating policy strategies for managing accounts receivable turnover. The inventory must be modified to meet the needs of pickier clients. As a result, the business may consider selecting potential clients to optimize anticipated profit and act as a guide for decision-making.

## 10. LIMITATIONS AND SUGGESTIONS FOR FUTURE STUDIES

Future research must account for all ratios in the research model, as this study does not cover all Bahraini industries. Due to the study's dependence on a single sample sector, the manufacturing industry, its findings are not more generalizable and may only apply to a subset of industries. Future investigations must account for the prospective sample size. The company's ability to generate a profit is influenced by its size. Future studies may utilize a product from the manufacturing industry and other companies listed on the Stock Exchange. Future research must also incorporate various profitability ratios, such as return on assets (NPM) and return on equity, to analyze the relationship between sales growth ratios (ITR), (ART), total asset turnovers, and growth potential objectively.

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