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THE ILLUSION OF PROFIT AND THE ULTIMATE REALITY OF CASH IN CORPORATE ORGANIZATIONS

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ABSTRACT

The concept of profit is often seen as the ultimate measure of success for a business. However, some argue that profit is merely an illusion and that cash is the ultimate reality in a business. This paper explores the idea that profit can be misleading and that cash flow is a more accurate measure of a company's financial health. Profit is defined as the difference between revenue and expenses over a specific period. However, this measure does not take into account the timing of cash inflows and outflows. A company may show a profit on its income statement, but if it has significant accounts receivable or inventory, it may not have enough cash to meet its current obligations. In contrast, cash flow is the movement of cash in and out of a business, and it reflects the actual cash available to a company at any given time. The paper argues that focusing solely on profit can lead to poor financial decision-making. For example, a company may pursue sales that generate a high profit margin but require significant upfront costs, resulting in negative cash flow. Conversely, a company may opt for lower-profit sales that generate immediate cash flow and are less risky. The paper also discusses how cash flow is critical in determining a company's ability to invest in growth opportunities, pay off debt, and distribute dividends to shareholders. A company with a positive cash flow has the financial flexibility to weather economic downturns, make strategic investments, and return value to its shareholders. In conclusion, profit is not a reliable indicator of a company's financial health, and cash flow is a more accurate measure of a company's ability to meet its financial obligations and pursue growth opportunities. While profit is essential, it should not be the sole focus of a company's financial strategy. Companies must prioritize cash flow management to ensure they have the resources to achieve long-term success.

Keywords: Profit, Illusion, Cash, Cash flow, Shareholder Wealth, Financial Risk, Financial Success.

1.0 INTRODUCTION

Profit and cash are two essential concepts in accounting, economics and finance globally. Although they are often used interchangeably, they however have distinct meanings. Profit refers to the surplus earned after all the expenses are subtracted from the revenue, while cash refers to the amount of money a company has in its bank account. While profit is an important metric for measuring the success of a business, it can be misleading at times. One of the primary goals of any business is to make a profit. Profit emanates from the concept of profitability. Profitability is the ability of a company to generate revenue that exceeds its costs and expenses. Profit is crucial to shareholders in a company because it is the primary source of return on investment (ROI). In this segment of the paper, attempt is made to aptly discuss the importance of profitability to shareholders in a company.

Conventionally, shareholders in a company will not smile at board of directors and other management team in the absence of profit or low profits made in a financial year based on certain fundamental reasons which among others include but not limited to shareholder wealth maximization, dividends, stock buy backs, future growth opportunities, and shareholder activism. In shareholder wealth maximization, the primary objective of a quoted company is to maximize shareholder wealth. Shareholder wealth can be seen as the value of a company's stock, which is determined by the price per share multiplied by the number of outstanding shares. A company's profitability has a direct impact on its stock price in the stock market. The higher the profitability of a company, the higher its stock price will be, which ultimately leads to increased shareholder’s wealth.

Dividends are a portion of a company's profits that are distributed to its shareholders. Companies that are profitable are more likely to pay dividends to their shareholders. Dividends are an essential source of income for many investors, particularly retirees who rely on their investments for income. Thus, profitability is crucial to shareholders who depend on dividends as a source of income.Stock buybacks are another way companies distribute profits to their shareholders. When a company buys back its own stock, it reduces the number of outstanding shares, which increases the value of the remaining shares. So, shareholders see profitability as crucial to a company's ability to repurchase its stock because it requires cash reserves.

Shareholders take profit seriously because of the need for a company’s future growth opportunities. A company's profitability is essential to its ability to invest in future growth opportunities. When a company is profitable, it can reinvest its profits into research and development, new products, and expanding into new markets. These investments can lead to increased revenue, which ultimately leads to increased profitability and shareholder wealth.Shareholder activism is the use of a shareholder's ownership stake in a company to influence its policies and practices. Shareholder activism is more likely to occur when a company is not profitable or not meeting its financial goals. Shareholders who are unhappy with a company's performance may try to influence management to take actions that increase profitability, such as cutting costs or increasing revenue.

Merits and Implications of Profits in Corporate Organizations

The generation of profits by a company commands some benefits and implications. Among the numerous benefits include creating a niche, securing loan facility, job security as well as promotes managers' assessment of the progress of a company for a financial year. Profit is crucial to creating a niche in the market. Companies that are profitable have the financial resources to invest in research and development, marketing, and advertising. This enables them to differentiate their products or services from their competitors and attract customers. Profitability also allows companies to offer competitive prices, which is a significant factor in creating a niche in the market. In the view of Prasetyo and Suryanto (2021), profits help companies to differentiate themselves from their competitors by offering better products and services. Companies that are profitable can invest in research and development to improve their products and services, which can attract more customers and increase their market share. Profit is essential to securing loans. Lenders want to ensure that a company has the ability to repay the loan. Profit is a key indicator of a company's ability to generate enough cash flow to repay the loan. Companies that are profitable have a higher chance of securing loans at favorable interest rates. Profit is an important factor in securing loans from banks and other financial institutions. According to a study by Alsharairi and Alghalith (2018), profitable companies are less risky and more attractive to lenders, making it easier for them to secure loans. Lenders are more likely to lend to companies that have a track record of profitability because they are confident that the companies will be able to repay the loans.

Profit is crucial to job security. Corporate organizations that are profitable have the financial resources to invest in their employees. This includes training, benefits, and competitive salaries. Profitable companies are also less likely to experience layoffs or downsizing, which creates job security for employees. Profitability is crucial for job security in a company. Terpstra and Rozell (2016) noted that profitable corporate organizations are more likely to retain their employees and offer better job security. Companies that are profitable have more resources to invest in employee training and development, which can improve job satisfaction and reduce turnover.

Profit is a significant factor in managerial assessment. Managers are responsible for the financial performance of their departments and the company as a whole. Managers who are successful in increasing profitability are seen as effective leaders. Profit is also used as a key performance indicator (KPI) in assessing managerial performance. Profit is also an important factor in managers' assessment. According to a study by Yeo and Ang (2020), managers who are able to increase profitability are more likely to be rewarded with promotions and bonuses. Companies that prioritize profitability in their performance evaluations are more likely to attract and retain top-performing managers.

While profit has many benefits, there are also implications that must be considered. One implication is that companies may prioritize profitability over other factors, such as ethical behavior and social responsibility. This can lead to negative consequences, such as environmental damage or labor exploitation. Another implication is that companies may focus on short-term profitability at the expense of long-term growth and sustainability.

The Illusion of Profit in Corporate Organizations

Profit can be an illusion because it does not reflect the actual cash flow of a business. A company can have high profitability on paper but struggle to pay its bills because it does not have the cash on hand to do so. This situation can arise when a company has a lot of accounts receivable, which represent revenue that has not been collected yet. If customers are slow to pay their bills, the company may struggle to pay its own bills. There are several reasons and criticisms on why profit is an illusion in a business. Some of these reasons and criticisms are the assumption that a company's revenue exceeds its costs and expenses. For example, the concept of profit is based on the assumption that a company's revenue exceeds its costs and expenses. However, this assumption does not take into account the true economic cost of a company's operations, such as the environmental and social impacts.

Critics argue that the pursuit of profit has led to environmental degradation, social inequality, and other negative externalities. Profit is an essential metric for measuring the success of a business. However, it can be misleading at times. The main reason for this is that profit is an accounting concept that is calculated by subtracting expenses from revenue. It does not reflect the actual amount of cash a company has in its bank account. For instance, a company may report a significant profit on its income statement, but it may not have enough cash to pay its bills. This situation can occur when a company has a lot of outstanding invoices or when it has invested a significant amount of money in assets that are not easily converted into cash.

Profit is seen as an illusion because of accounting practices. Accounting practices have a significant impact on a company's reported profit. One example is the use of depreciation, which is the process of spreading the cost of an asset over its useful life. Depreciation can artificially lower a company's expenses and increase its reported profit. Another example is the use of tax loopholes and accounting tricks to minimize tax liability, which can also inflate reported profits. Another issue with profit is that it can be manipulated. Some corporate organizations may use creative accounting practices to inflate their profits artificially. For example, a company may delay recording expenses or accelerate revenue recognition to make its profit look better than it actually is. Therefore, relying solely on profit as a measure of a company's financial health can be risky. It is essential to consider other factors such as cash flow, liquidity, and solvency when evaluating a company's financial performance.

Most corporate organizations often focus on short-termism in terms of profit making. Many companies focus on short-term profitability at the expense of long-term sustainability. This short-term focus can lead to decisions that benefit shareholders in the short term but harm the company's long-term prospects. For example, a company may cut research and development spending to boost short-term profits, but this can lead to a lack of innovation and reduced competitiveness in the long term. The concept of shareholder value maximization is often cited as a reason why profit is an illusion. The idea is that companies should prioritize the interests of shareholders above all else, even if this means sacrificing other stakeholders' interests, such as employees, customers, and the environment. Critics argue that this narrow focus on shareholder value ignores the broader social and environmental impacts of business operations. Some researchers argue that alternative metrics, such as the triple bottom line (TBL), provide a more comprehensive view of a company's economic reality. The TBL considers not only financial performance but also social and environmental impacts.

Companies that prioritize sustainability and social responsibility may be more likely to succeed in the long term than those focused solely on profit.

Cash as King and the Ultimate Reality in Corporate Organizations

Cash is more superior because it is the lifeblood of any corporate organizations globally. It is essential for paying bills, buying inventory, and investing in new opportunities. Without cash, a company cannot survive, no matter how profitable it appears to be. Cash flow is the amount of cash that flows in and out of a company over a specific period. It is a more accurate measure of a company's financial health than profit. Positive cash flow means that a company has enough cash to cover its expenses and invest in its growth. On the other hand, negative cash flow indicates that a company is struggling to pay its bills and may need to borrow money to stay afloat. Therefore, it is essential to focus on cash flow when evaluating a company's financial performance.

Furthermore, cash can be seen as king and the ultimate reality in a business because it represents the actual money that a company has available to pay its expenses, invest in new projects, and distribute to shareholders. In the context of this paper, the major reasons on why cash is the ultimate reality in a business are primarily premised on liquidity and profitability, cash flow management, investment opportunities and shareholders value. One of the most important reasons why cash is king and the ultimate reality in corporate organizations is because it is a measure of a company's liquidity and financial stability. Companies with a high level of cash reserves are better positioned to weather financial downturns, pay their bills, and meet their obligations. In a study by Hill, Kelly, and Lockhart (2017), they found that companies with higher levels of cash reserves had a lower probability of financial distress. Effective cash flow management is critical to the success of any business. Companies that have a good understanding of their cash inflows and outflows are better positioned to make informed decisions about how to allocate resources. According to a study by Mamun, Nath, and Uddin (2019), companies that manage their cash flow effectively are more likely to have higher profitability and shareholder value.

Cash is also crucial to a company's ability to invest in new projects and opportunities. Companies with high levels of cash reserves are better positioned to take advantage of new investment opportunities, as they have the funds available to make investments without having to rely on external sources of funding. In a study by Deli, Kulathunga, and Xiao (2016), they found that cash-rich companies were more likely to make acquisitions, invest in research and development, and increase their capital expenditures. Cash is also important to a company's ability to create shareholder value. Companies that generate excess cash are better positioned to distribute that cash to shareholders in the form of dividends or share buybacks. In a study by Han, Li, and Li (2015), they found that companies that distributed cash to shareholders had higher stock prices and increased shareholder value.

Superiority of Cash over Profit in Corporate Organizations

Many people, including financial managers do believe that a company's profitability is the most crucial measure of success. However, this belief is misguided, and profit is actually an illusion. Profit is a theoretical concept that does not reflect the cash flow of a business, and cash flow is the ultimate reality that determines the success or failure of a company. Similarly,

profit is a theoretical concept that represents the difference between revenue and expenses. Profitability measures how efficiently a company is using its resources to generate revenue. However, profitability does not reflect the company's cash flow. Cash flow represents the amount of cash that is coming into and going out of a business. Cash flow is the ultimate reality because it determines a company's ability to pay its bills, invest in new projects, and survive economic downturns.

Thus, the imperativeness of cash over profit in corporate organizations cannot be over emphasized. Cash is essential to a business because it provides the resources to invest in new projects, pay employees and suppliers, and weather economic downturns. Companies that have high profitability but low cash flow can struggle to stay afloat because they may not have the cash on hand to pay their bills. Conversely, companies with low profitability but high cash flow can survive economic downturns and invest in new projects because they have the resources to do so. Managing cash flow is critical to the success of a business. Companies can manage their cash flow by monitoring their accounts receivable and accounts payable, creating a budget, and forecasting cash flow. By managing their cash flow, companies can ensure that they have the resources to pay their bills, invest in new projects, and survive economic downturns.

Theoretical Framework

Some theories suggest that profit may be an illusion and that cash flow is the ultimate reality in a business. This paper uses the cash flow theory, free cash flow theory, time value of money theory, earnings management theory and business cycle theory, and cash conversion cycle theory to assess how profit is an illusion and cash is the ultimate reality in a business. The cash flow theory asserts that cash flow, not profit, is the ultimate measure of a company's financial health. The reasoning behind this is that profit is merely an accounting concept that does not necessarily reflect the actual cash that a company has on hand. In contrast, cash flow reflects the actual inflows and outflows of cash, which is critical for a company's ability to pay its bills, invest in growth, and meet its financial obligations. Time value of money theory argues that cash is more valuable than profit because of the time value of money. Money has a time value because it can earn interest or be invested to generate future cash flows. Thus, a dollar today is worth more than a dollar tomorrow. Profit is a measure of the excess revenue over expenses during a period, but it does not take into account the time value of money. In contrast, cash on hand can be invested to generate future returns, making it more valuable than profit.

Earnings management theory suggests that profit can be manipulated by managers to meet financial targets, which may not reflect the true financial health of a company. For example, a company may use accounting methods to inflate its revenue or defer expenses to artificially boost profits. In contrast, cash is more difficult to manipulate and reflects the actual financial position of a company. Furthermore, the earnings management theory suggests that profit may be an illusion because companies can manipulate their earnings to make them appear more favorable than they actually are. Companies can use various accounting techniques to inflate their earnings temporarily, such as recognizing revenue before it is earned or delaying expenses. However, these techniques do not reflect a company's actual cash flow position, and in the long run, they can damage a company's financial health. (Brigham & Ehrhardt, 2014)

Business cycle theory argues that profit is subject to economic cycles and market fluctuations, which can make it an unreliable measure of a company's financial health. During economic downturns, for example, a company may experience declining profits even if its cash position remains strong. In contrast, cash on hand provides a more stable and reliable measure of a company's ability to weather economic storms and meet its financial obligations. The cash conversion cycle (CCC) theory argues that cash is the ultimate reality in a business because it represents the amount of time it takes for a company to convert its investments in inventory and accounts receivable into cash. The shorter the CCC, the better a company's cash flow position, and the more likely it is to be financially healthy. According to this theory, profit may be an illusion because it does not necessarily reflect a company's ability to convert its investments into cash. (Hillier et al., 2017)

2.0 CONCLUSION AND RECOMMENDATIONS

This paper has examined and argued on why profit is an illusion and cash is the main reality in a business enterprise. Profit is an essential metric for measuring the success of a business, but it can be misleading at times. Cash is the ultimate reality in business finance because it is essential for a company's survival. Without cash, a company cannot pay its bills or invest in its growth, no matter how profitable it appears to be. In conclusion, profitability is essential to the success and survival of any business. It allows companies to create a niche in the market, secure loans, provide job security for employees, and assess managerial performance. However, it is important to consider the implications of prioritizing profitability over other factors, such as ethical behaviour and long-term growth. In conclusion, cash is the ultimate reality in a business because it is a measure of a company's liquidity and financial stability, is crucial to effective cash flow management, enables investment opportunities, and creates shareholder value. Companies that prioritize cash management and maintain high levels of cash reserves are better positioned to weather financial downturns, invest in new projects, and create value for shareholders.

Based on the literature explored, this research paper suggests that:

i. Business owners and managers must understand the difference between profit and cash flow and the importance of managing both effectively.
ii. Businesses should focus on managing their cash flow effectively to ensure their financial stability and long-term success. This includes managing accounts receivable and payable, forecasting cash flow, and maintaining adequate cash reserves.
iii. While profit is a useful tool to measure a business's financial performance, it should not be the ultimate measure. Businesses should use profit in conjunction with other measures, such as cash flow and return on investment, to make informed decisions.
iv. Businesses should avoid aggressive accounting practices that manipulate profits and obscure the true financial position of the company. Instead, they should adopt transparent and ethical accounting practices that accurately reflect their financial performance.
v. Business owners and managers should seek professional advice from financial experts, such as accountants and financial advisors, to ensure that they are managing their finances effectively and making informed decisions. By following

these recommendations, businesses can ensure that they are managing their finances effectively and prioritizing cash flow over profit, thereby ensuring their long-term success

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