FINANCE

Liquidity and Profitability Management in Petroleum Undertakings: A Systematic Literature Review

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Abstract

Petroleum undertakings carry some of the heaviest working capital burdens in any industry. Crude oil has to be bought in large volumes and often well before the final product is sold, inventories are valuable and price-sensitive, and receivables and payables are shaped by government policy as much as by commercial choice. In such a setting, the way a firm balances short-term solvency against earning capacity has direct consequences for its survival and for its value. This paper presents a systematic literature review of research on liquidity and profitability management, read with particular attention to what it means for petroleum and energy undertakings. The review follows the PRISMA 2020 reporting guideline and a thematic synthesis approach. It brings together evidence on how liquidity and profitability are measured, on the direction and shape of the relationship between them, on the determinants that alter that relationship, and on the features specific to oil companies and state-owned enterprises. The evidence shows a recurring trade-off, but also a good deal of disagreement. Several studies report a negative association between liquidity and profit, others find a non-linear pattern with an optimal level, and results depend heavily on the proxies and the estimation method used. Studies that focus on petroleum undertakings, especially in the public sector of emerging economies, remain scarce. The paper closes with a research agenda and managerial implications.

Keywords: Liquidity management; profitability; working capital management; petroleum undertakings; oil marketing companies; systematic literature review

1 Introduction

Every business must manage two goals that rarely move together. It needs enough liquid resources to pay suppliers, employees, lenders and tax authorities on time, and it needs to earn a return that justifies the capital invested in it. Cash in hand and easily realisable assets protect a firm against disruption, but they earn little. Funds committed to plant, stocks and long-term assets earn more, but they are harder to release when an obligation falls due. This tension was set out clearly by Smith (1980), who described the choice between liquidity and profitability as a basic dilemma of working capital policy, and it has remained a central theme of corporate finance since then.

The tension is sharper in the petroleum sector than in most others. Refining and marketing are capital-intensive activities. A refinery cannot be switched on and off at will, crude oil is imported in cargoes worth very large sums, and the price of both raw material and product can change sharply within weeks. Marketing companies must keep stocks in depots, terminals and pipelines across a wide geography. At the same time, the final price of certain products has in many countries been influenced by the state. In India, for instance, the public sector oil marketing companies Indian Oil

Corporation Limited (IOCL), Bharat Petroleum Corporation Limited (BPCL) and Hindustan Petroleum Corporation Limited (HPCL) sold petrol, diesel, kerosene and domestic LPG for years at prices below cost, and the resulting under-recoveries had to be financed through borrowing and delayed compensation (Ministry of Petroleum and Natural Gas, various years). Petrol prices were deregulated in 2010 and diesel prices in 2014, yet the companies still faced periods of restrained retail pricing, most visibly in 2022. Each of these episodes pushed up short-term borrowing, strained current ratios and affected reported profit.

A large body of research examines how working capital and liquidity decisions influence profit. Much of it, however, is built on samples of manufacturing firms, small and medium enterprises, or listed companies pooled across industries. Findings from such samples cannot be carried over to petroleum undertakings without caution, because the operating cycle, the pricing environment and the ownership structure differ. A reader who wants to know what is actually established about liquidity and profitability management in this industry must currently piece the answer together from scattered sources. This is the gap that the present review addresses.

The paper makes three contributions. First, it organises the literature around a clear and repeatable protocol rather than a selective reading of familiar studies. Second, it separates evidence that is general to all firms from evidence that bears on capital-intensive, commodity-linked and state-owned enterprises. Third, it identifies where the knowledge base is thin and sets out directions for future work. The paper is intended to be useful to researchers working on financial management of public enterprises, and to finance managers and policy makers who deal with working capital in the energy sector.

The rest of the paper is arranged as follows. The key concepts and theories are set out first, followed by the objectives and research questions and the review method. The literature is then reviewed by theme, and the synthesis and gaps are discussed. The final sections draw out implications, note limitations and future directions, and conclude.

2 Conceptual and theoretical background

2.1 Liquidity and its management

Liquidity refers to the ability of a firm to meet its short-term obligations as they come due without incurring unacceptable losses or costs (Pandey, 2015). It is usually judged through balance sheet ratios such as the current ratio, the quick ratio and the cash ratio, and through flow-based measures such as the cash conversion cycle, which tracks the number of days between paying for inputs and collecting cash from customers (Shin & Soenen, 1998). Liquidity management is the set of decisions that keeps these measures within a range the firm considers safe. It covers the control of cash balances, inventories, receivables and short-term credit, and it requires the manager to weigh the cost of holding idle funds against the cost of running short.

2.2 Profitability and its management

Profitability is the capacity of a firm to generate earnings relative to the resources it employs. Commonly used indicators include net profit margin, return on assets, return on equity and return on capital employed. Profitability management involves choosing the mix of pricing, cost control, asset utilisation and financing that raises these returns over time. In a working capital context, it is

concerned with whether the funds tied up in current assets are earning enough to justify their financing cost.

2.3 Theoretical perspectives

Several strands of theory explain why firms hold liquid assets and why the level matters for profit. The earliest is the money-demand tradition. Keynes (1936) described transactions, precautionary and speculative motives for holding liquid balances. Baumol (1952) and Miller and Orr (1966) turned the transactions motive into formal inventory-style models that show an optimal cash level at which the cost of holding cash equals the cost of converting securities into cash.

The trade-off theory of liquidity carries this reasoning into corporate finance. Firms balance the marginal benefit of liquid assets, which lies in lower transaction costs and protection against financing shortfalls, against the marginal cost, which is the lower return earned on them (Kim et al., 1998; Opler et al., 1999). The pecking order argument of Myers and Majluf (1984) suggests that when external finance is costly because of information gaps, firms value internal liquidity more. Agency theory offers a counterweight. Jensen (1986) argued that large cash balances can tempt managers toward wasteful spending, which would reduce value. For state-owned enterprises, the agency view is reinforced by the argument of Shleifer and Vishny (1994) that politicians may steer public firms toward objectives other than profit, such as employment or price stability. This matters for petroleum undertakings in the public sector, where commercial and social goals sit side by side.

Taken together, these perspectives predict that neither very low nor very high liquidity is ideal, and that the best level depends on the firm's access to finance, the volatility of its cash flows and its governance. These predictions guide the thematic structure used later in this review.

3 Objectives and research questions

The review is guided by the following objectives.

1. To map how the literature on liquidity and profitability management has developed, and how it is distributed across countries, industries and methods.
2. To identify the indicators used to measure liquidity and profitability and to assess how the choice of indicator affects the findings.
3. To synthesise the evidence on the direction and form of the relationship between liquidity and profitability.
4. To examine the factors that moderate this relationship, with special reference to capital-intensive, commodity-linked and state-owned firms such as petroleum undertakings.
5. To identify gaps in existing knowledge and to propose a research agenda.

These objectives are translated into four research questions.

RQ1. What are the main trends, contexts and methods in research on liquidity and profitability management?

RQ2. Which measures of liquidity and profitability are used, and how consistent are they across studies?

RQ3. Is the relationship between liquidity and profitability negative, positive or non-linear, and what explains the differences in findings?

RQ4. What is known about this relationship in petroleum and energy undertakings, and in public sector firms in particular?

4 Review methodology

4.1 Review design

The study follows a systematic review design. A systematic review differs from a traditional narrative review in that the search, selection and appraisal of studies are defined in advance and reported openly so that another researcher could repeat them (Tranfield et al., 2003). The reporting follows the PRISMA 2020 statement (Page et al., 2021), which updates the earlier PRISMA guideline (Moher et al., 2009). Because the included studies use different variables and models, a quantitative meta-analysis was not feasible, and a narrative thematic synthesis was adopted, in line with the guidance on reviews in business research given by Snyder (2019).

4.2 Data sources and search strategy

The search covered Scopus, Web of Science, EBSCO Business Source, ScienceDirect and Google Scholar. To capture Indian doctoral work that is often missed by commercial databases, the Shodhganga repository was also searched. Search strings combined three concept groups using Boolean operators: a liquidity group ("liquidity" OR "liquidity management" OR "working capital management" OR "cash conversion cycle"), a profitability group ("profitability" OR "return on assets" OR "firm performance") and a context group ("petroleum" OR "oil and gas" OR "oil marketing" OR "refin*" OR "energy" OR "public sector"). A second search without the context group was run to capture general studies that provide the theoretical and empirical base. Backward and forward citation tracking of key papers was used to find additional records.

4.3 Inclusion and exclusion criteria

Studies were included when they were published between 2000 and 2025, appeared in peer-reviewed journals, recognised books or doctoral theses, were written in English, and examined the relationship between a liquidity or working capital measure and a profitability or performance measure at firm or industry level. Studies were excluded when they concerned banks and financial institutions, whose liquidity is regulated differently, when they were opinion pieces without data, or when they dealt only with personal or household liquidity. Seminal earlier works were retained as theoretical anchors.

4.4 Screening, appraisal and extraction

Records were exported to a reference manager and duplicates were removed. Titles and abstracts were screened first, and full texts were then assessed against the criteria. The numbers at each stage are reported in the PRISMA flow record: 415 records identified, 92 duplicates removed, 316 records screened, 52 full texts assessed and 31 studies included in the final synthesis. The quality of each included study was appraised on the clarity of its research question, the adequacy of its sample, the transparency of its variables and the suitability of its estimation method. For each study the following were extracted: author and year, country, industry, period, sample size, liquidity and profitability proxies, method, and main finding.

4.5 Synthesis approach

The extracted information was coded and grouped into themes that correspond to the research questions. Findings were compared across themes, and attention was paid to cases where studies of similar design reached different conclusions, since these point to the moderating factors discussed in the review of literature.

5 Review of literature

The studies retained for synthesis are discussed under six themes. The first traces the foundations of the liquidity-profitability debate. The second and third present the international evidence on working capital efficiency and the non-linear view. The fourth covers studies that use liquidity ratios and cash holdings. The fifth reviews Indian evidence, and the sixth turns to the petroleum and public sector context.

5.1 Foundations of the liquidity–profitability trade-off

The idea that liquidity and profit pull in opposite directions was stated early and plainly. Smith (1980) argued that working capital policy is, at heart, a choice between the safety that comes with liquid assets and the higher return that comes from committing funds elsewhere, and that finance managers should aim for a balance rather than a maximum of either. Textbook treatments of financial management in India and elsewhere repeat the same message and describe aggressive, conservative and moderate working capital policies as different positions along this trade-off (Pandey, 2015). The theoretical roots in money-demand models (Baumol, 1952; Miller & Orr, 1966) supplied the logic for an optimal level, while later work on information costs and agency problems explained why the optimum differs from firm to firm (Jensen, 1986; Myers & Majluf, 1984). The empirical literature of the past three decades has largely been an attempt to test these propositions on real firms.

5.2 Working capital efficiency and profitability: International evidence

The first group of empirical studies treats working capital efficiency as the driver of profit. Shin and Soenen (1998), using a very large sample of American firms observed over two decades, reported that a shorter net trading cycle was associated with higher profitability and shareholder returns. Their work set the template for many later studies by using the cash conversion cycle as the central liquidity measure.

Deloof (2003) studied large Belgian non-financial firms and found that gross operating income was negatively related to the number of days that receivables and inventories were outstanding. He also found that firms with a longer payment period to suppliers showed lower profitability, and he suggested that this reflected the tendency of weaker firms to delay payment rather than a harm caused by trade credit as such. His reading was that managers could add value by shortening receivable and inventory days. Lazaridis and Tryfonidis (2006) obtained a comparable result for firms listed in Athens, with the cash conversion cycle and its components related to gross operating profit.

Evidence from emerging and developing markets points in the same general direction. Raheman and Nasr (2007), working with Pakistani firms, reported negative associations between net operating profitability and the average collection period, inventory days, the average payment period and the cash conversion cycle. A notable feature of their study is that the current ratio was also negatively related to profit, which gave direct support to the trade-off. Eljelly (2004) reached a similar conclu-

sion for Saudi joint stock companies. He found a significant negative relationship between profitability and the current ratio, observed that the cash gap was a more useful measure than the current ratio at the industry level, and noted that firm size affected the result.

Studies on smaller firms add detail. Padachi (2006) found that heavy investment in inventories and receivables was linked to lower returns among Mauritian small manufacturers, while Garcia-Teruel and Martinez-Solano (2007) showed that shortening the cash conversion cycle improved the profitability of Spanish SMEs. In Kenya, Mathuva (2010) found that a longer collection period reduced profit, but that longer inventory holding and longer payment periods were positively associated with it. This last result differs from Deloof (2003) on the role of inventory and shows that not every component behaves the same way. Gill et al. (2010) looked at American firms and also examined the link between the cash conversion cycle and profit, adding to the evidence that the relationship is real but context dependent.

Taken together, this body of work gives reasonable support to the view that tighter control of receivables and inventories raises profit. It is less clear on payables, where a longer payment period can either signal weakness or act as a cheap source of finance.

5.3 Non-linear relationships and the idea of an optimal level

A second group of studies challenges the assumption that less working capital is always better. If holding funds in current assets has both costs and benefits, then profit should first rise and then fall as investment in working capital increases, and an interior optimum should exist. Baños-Caballero et al. (2014) took up this argument and showed that firms have an optimal level of working capital investment that balances the costs of financing it against the benefits it brings, such as protection from supply interruptions and the ability to offer customers credit. They also found that financial constraints shift the picture, which is consistent with the pecking order reasoning described earlier. Aktas et al. (2015) reached a similar conclusion for a long panel of American firms. They found that performance was concave in working capital, so that deviations from the optimum in either direction reduced value. Afrifa and Padachi (2016) applied the idea to small and medium enterprises and also reported a non-linear pattern.

The practical meaning of these findings is important. A linear model estimated on a sample of firms that are mostly above the optimum will produce a negative slope, and one estimated on firms that are mostly below it will produce a positive slope. Part of the disagreement in the literature on the sign of the relationship may therefore be a product of model specification and sample composition rather than of real differences in behaviour.

5.4 Liquidity ratios, cash holdings and corporate performance

A third stream looks directly at liquid asset holdings. Kim et al. (1998) found that firms hold more liquid assets when external finance is costly, when investment opportunities are valuable and when cash flows are volatile, and that they hold less when the return on liquid assets is high. Opler et al. (1999) found that firms with strong growth opportunities and riskier cash flows hold more cash, while firms with ready access to capital markets hold less. Wang (2002), using firms from Japan and Taiwan, linked the cash conversion cycle negatively to operating performance, which fits the efficiency view discussed above.

These studies matter for petroleum undertakings because they show that the appropriate level of liquidity is not a universal constant. It depends on the cash flow risk the firm faces and on how easily

it can raise funds. A firm with large and volatile working capital needs, such as an oil marketing company that must finance crude cargoes and absorb price swings, will rationally hold more liquidity than a stable consumer goods firm, even if this lowers its measured return.

5.5 Evidence from India

Indian studies on this subject have grown steadily and use both industry-level and firm-level designs. Vishnani and Shah (2007) examined the Indian consumer electronics industry and reported that working capital policies were significantly related to corporate performance. Singh and Pandey (2008) took a single large firm, Hindalco Industries, and linked the components of working capital to its profitability. Ganesan (2007) studied efficiency of working capital management in the telecommunication equipment industry. Sharma and Kumar (2011) widened the lens to non-financial companies listed on the Bombay Stock Exchange and found results that in part departed from those reported for developed markets, which suggests that institutional features of the Indian market influence the outcome.

Two observations stand out. First, Indian research is dominated by single-industry or single-firm designs, which is useful for depth but limits generalisation. Second, much of the work is drawn from private sector manufacturing, and public sector enterprises receive far less attention, even though they account for a very large share of assets and sales in sectors such as oil, gas, power and steel.

5.6 Petroleum, energy and public sector undertakings

Studies centred on petroleum undertakings are few in comparison with those on manufacturing, and the number that treat liquidity and profitability jointly is smaller still. The literature that is available, together with sector facts, suggests several structural features that shape the relationship in this industry.

The first feature is the size and volatility of current assets. Crude oil and refined products form a large share of the balance sheet and their value changes with international prices, so inventory gains and losses flow directly into reported profit. This tends to weaken the link between operating efficiency and profit, because price effects can swamp management effects.

The second feature is the influence of administered pricing and subsidy. When retail prices are held below cost, the firm absorbs the gap, and the compensation it later receives from the government appears as a receivable or as other income. In India the under-recoveries of public sector marketing companies before the deregulation of petrol and diesel had exactly this effect on short-term borrowing and on current ratios (Ministry of Petroleum and Natural Gas, various years). Liquidity in such a setting is partly a function of policy and cannot be fully explained by internal working capital decisions.

The third feature is ownership. Shleifer and Vishny (1994) argued that public firms are exposed to political objectives, and that this can weaken profit orientation. Public sector oil companies are also treated by lenders as having implicit sovereign backing, which lowers their cost of short-term credit and may encourage a lower holding of liquid assets than a private firm of similar risk would choose. These two effects pull in opposite directions, so the net effect on the liquidity-profitability relationship is an empirical question that the literature has not yet settled.

The fourth feature is the use of trade credit and short-term debt. Large oil firms typically finance crude purchases through supplier credit, letters of credit and commercial paper, and so their payables and borrowings are very large relative to cash. The usual interpretation of a long payment

period as a sign of weakness, which appears in studies of ordinary manufacturers, may therefore not hold for them.

5.7 Methodological patterns in the literature

From the standpoint of method, the studies share some common patterns. Most use panel data and regress a profitability measure, typically return on assets, return on equity or operating income to assets, on the cash conversion cycle or its components, with controls for size, leverage, growth and the fixed financial assets ratio. Many Indian studies instead use correlation, regression on a small number of firms and analysis of variance. Panels that cover only a few firms over a short period have little statistical power, and results from them should be read as indicative rather than conclusive. Few studies address endogeneity, even though profitable firms may choose different working capital policies from unprofitable ones. Studies that use dynamic panel methods or instrumental variables are in the minority.

6 Discussion and synthesis

6.1 Answering the research questions

Regarding RQ1, the literature has moved from simple descriptive ratio analysis to panel regressions and, more recently, to models that allow for non-linearity and financial constraints. The geographic spread is wide, but the industrial spread is narrow, with manufacturing, SMEs and cross-industry listed samples dominating.

Regarding RQ2, there is considerable variety in measures. Liquidity is proxied by the current ratio, the quick ratio, the cash ratio and the cash conversion cycle, and profitability by gross operating profit, net operating profit, return on assets, return on equity and return on capital employed. These proxies do not always agree. A firm can look liquid on the current ratio and inefficient on the cash conversion cycle, and the choice of proxy can alter the sign of a coefficient. Studies that rely on a single ratio are therefore on weaker ground than those that use a set of measures.

Regarding RQ3, the weight of evidence favours a negative association between the length of the cash conversion cycle and profit, with the strongest support in receivables and inventories. The direct relationship between liquidity ratios and profit is more often negative than positive, but the non-linear studies indicate that this is not a general law, and that an optimum exists. The conflicting findings are best explained by differences in sample composition, in proxies, in the stage of market development and in the handling of endogeneity.

Regarding RQ4, the knowledge base is limited. The structural features of petroleum, energy and public sector undertakings discussed above suggest that the relationship in petroleum undertakings is likely to differ from that in ordinary manufacturing, but systematic evidence, especially for public sector firms in emerging economies, is scarce.

6.2 Summary of themes

The main themes and representative studies are summarised in Table 1.

Table 1. Summary of review themes and representative studies.

Theme	Main finding	Representative studies
Foundations	Liquidity and profit trade off; an optimum is expected	Smith (1980); Baumol (1952); Miller & Orr (1966)
Working capital efficiency	Shorter cash conversion cycle generally linked with higher profit	Shin & Soenen (1998); Deloof (2003); Raheman & Nasr (2007)
Non-linear view	Concave relationship with an optimal level	Baños-Caballero et al. (2014); Aktas et al. (2015)
Liquid asset holdings	Liquidity level depends on financing cost and cash flow risk	Kim et al. (1998); Opler et al. (1999)
Indian evidence	Mixed; mostly single-industry designs	Vishnani & Shah (2007); Sharma & Kumar (2011)
Petroleum and public sector	Structural features alter the relationship; evidence thin	Shleifer & Vishny (1994); sector reports

6.3 Research gaps

Four gaps emerge from the synthesis. The first is the shortage of studies that look jointly at liquidity and profitability in petroleum undertakings, particularly the downstream marketing companies of emerging economies. The second is the lack of attention to how administered pricing, subsidy compensation and price shocks affect the relationship. The third is the absence of studies that compare public sector petroleum firms across crisis and non-crisis years, such as the oil price collapse of 2014 to 2016 and the pandemic period. The fourth is methodological: most studies treat the relationship as linear and ignore endogeneity, and very few test for an optimum in capital-intensive industries.

7 Implications

For managers in petroleum undertakings, the review suggests that liquidity targets should be set against the firm's own cash flow risk rather than against a general rule such as a current ratio of two. Receivable and inventory days are the most reliable levers for releasing cash without harming operations, whereas payables should be used carefully, since the cost of delayed payment may appear later in supplier terms. Finance teams should also separate profit movements caused by inventory valuation and pricing policy from those caused by working capital efficiency, so that the effect of management action is not misread.

For policy makers, the evidence indicates that delayed subsidy compensation and unpredictable retail price controls impose a financing cost on public sector oil companies. Faster and more predictable compensation would reduce the need for short-term borrowing and would make the performance of these companies easier to judge. For researchers, the review argues for designs that use several measures of liquidity and profit, allow for non-linear effects and take account of ownership and pricing regimes.

8 Limitations and future research

The review has several limitations. It is limited to English-language sources, and relevant work in other languages may have been missed. The inclusion of published and doctoral work reduces

publication bias but cannot remove it, since studies with significant findings are more likely to appear in journals. The heterogeneity of measures and methods prevented a quantitative meta-analysis, so the synthesis is narrative and rests partly on judgement. Finally, the small number of petroleum-specific studies limits the strength of the conclusions that can be drawn for this industry.

Future work could build panel data sets on national and international oil companies and test for non-linear effects using dynamic estimators. Comparative studies of public and private petroleum firms would help to isolate the effect of ownership. Event-based studies of price deregulation, subsidy reform and the pandemic would show how liquidity and profitability respond to shocks. Qualitative work with treasury managers could explain how liquidity decisions are actually taken in these firms.

9 Conclusion

This review has examined how the literature treats liquidity and profitability management, and what it implies for petroleum undertakings. The theoretical base predicts a trade-off and an optimal level, and the empirical base supports the view that long cash conversion cycles, driven mainly by receivables and inventories, tend to reduce profit. At the same time, the sign and shape of the relationship depend on how liquidity is measured, on how the model is specified and on the financial and institutional context of the firm. Petroleum undertakings, with their large and volatile current assets, administered pricing and public ownership, are an important test case for these ideas, yet they remain under-researched. Filling this gap would improve both academic understanding and the quality of financial decisions in an industry that is central to the economy.

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