SOS POLITICAL SCIENCE AND PUBLIC ADMINISTRATION
MBA FA 403
SUBJECT NAME: WORKING CAPITAL MANAGEMENT

TOPIC NAME: WORKING CAPITAL

MEANING:

- Working capital, also known as net working capital (NWC), is the difference between a company’s current assets, such as cash, accounts receivable (customers’ unpaid bills) and inventories of raw materials and finished goods, and its current liabilities, such as accounts payable. Net operating working capital is a measure of a company's liquidity and refers to the difference between operating current assets and operating current liabilities. In many cases these calculations are the same and are derived from company cash plus accounts receivable plus inventories, less accounts payable and less accrued expenses.
- Working capital is a measure of a company's liquidity, operational efficiency and its short-term financial health. If a company has substantial positive working capital, then it should have the potential to invest and grow. If a company's current assets do not exceed its current liabilities, then it may have trouble growing or paying back creditors, or even go bankrupt.

- A company has negative working capital If the ratio of current assets to liabilities is less than one.
- Positive working capital indicates that a company can fund its current operations and invest in future activities and growth.
- High working capital isn't always a good thing. It might indicate that the business has too much inventory or is not investing its excess cash.

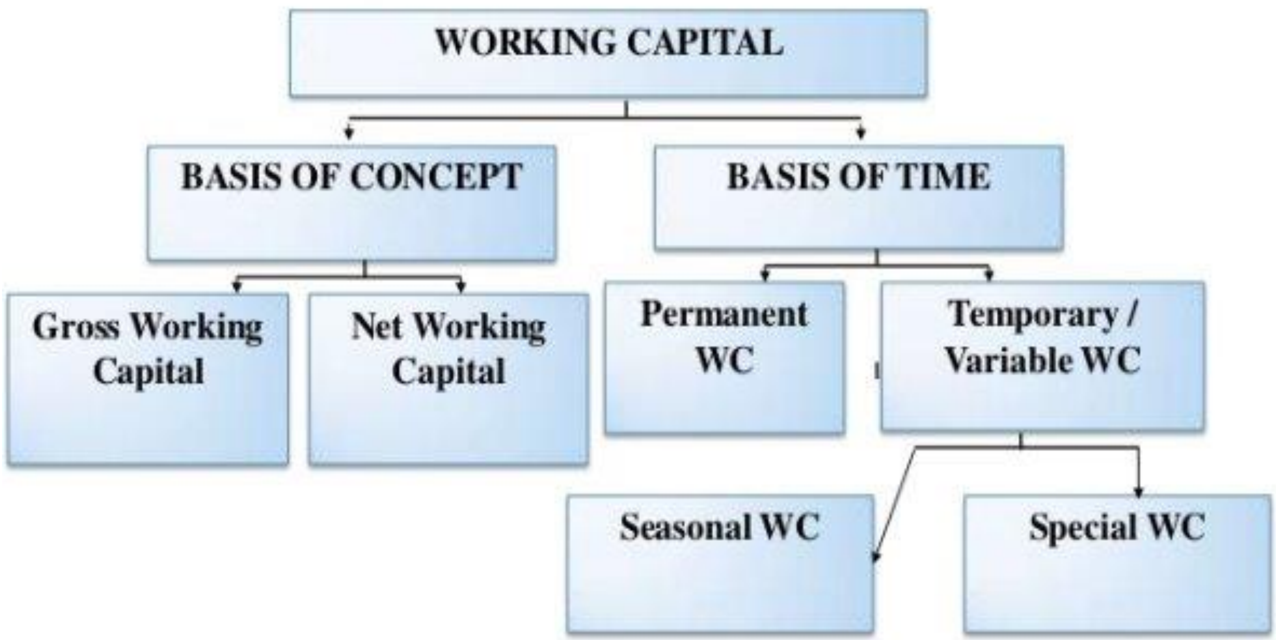
THE FORMULA FOR WORKING CAPITAL:

- To calculate the working capital, compare a company's current assets to its current liabilities. Current assets listed on a company's balance sheet include cash, accounts receivable, inventory and other assets that are expected to be liquidated or turned into cash in less than one year. Current liabilities include accounts payable, wages, taxes payable, and the current portion of long-term debt. Current assets are available within 12 months. Current liabilities are due within 12 months.
- The standard formula for working capital is current assets minus current liabilities.
- Working capital that is in line with or higher than the industry average for a company of comparable size is generally considered acceptable. Low working capital may indicate a risk of distress or default.

CHARACTERISTICS OF WORKING CAPITAL

- The aspect of Working Capital different it from the fixed capital are as follows:
- Short term needs.
- Circular movement.
- An element of permanency.
- An element of fluctuation.
- Less risky.
- Liquidity..
- Different proportion for each industry.

TYPES OF WORKING CAPITAL



COMPONENTS OF WORKING CAPITAL:

1. Cash Management:

- Cash is one of the important components of current assets. It is needed for performing all the activities of a firm, i.e. from acquisition of raw materials to marketing of finished goods. Therefore it is essential for a firm to maintain an adequate cash balance. One of the important functions of a finance manager is to match the inflows and outflows of cash so as to maintain adequate cash.

2. Receivables Management:

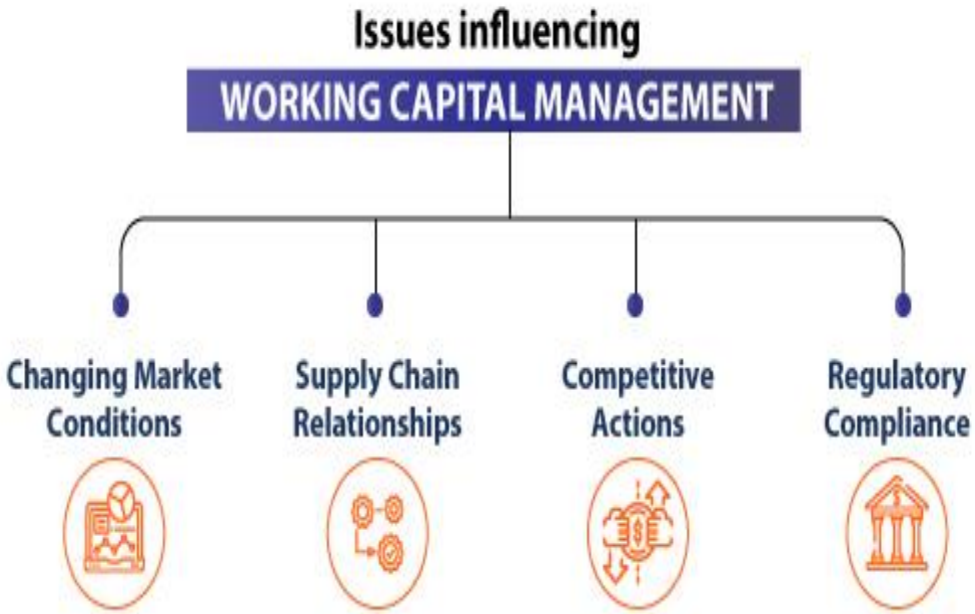
- The term receivable is defined as any claim for money owed to the firm from customers arising from sale of goods or services in normal course of business. The term account receivable represents sundry debtors of a firm. It is one of the significant components of working capital next to cash and inventories.
- The total volume of accounts receivable depends on its credit sale and debt collection policy—these two significantly influence the requirement of working capital. Liberal credit policy increases the volume of sales but at the same time it also increases the investment in receivables. Therefore, examination of costs and benefits associated with credit policy is one of the important tasks of a finance manager.

3. Inventory Management:

- Inventory constitutes a major part of total working capital. Efficient management of inventory results in maximization of earnings of the shareholders. Efficient inventory management consists of managing two conflicting objectives: Minimization of investment in inventory on the one hand; and maintenance of the smooth flow of raw materials for production and sales on the other.
- Therefore the objective of a finance manager is to calculate the level of inventory where these conflicting interests are reconciled. Like cash, a firm holds inventory for transaction, precautionary and speculative motives.

4. Accounts Payable Management:

- Payables or creditors are one of the important components of working capital. Payables provide a spontaneous source of financing of working capital. Payable management is very closely related with the cash management. Effective payable management leads to steady supply of materials to a firm as well as enhances its reputation.
- It is generally considered as a relatively cheap source of finance as suppliers rarely charge any interest on the amount owed. However, trade creditors will have a cost as a result of loss of enjoying cash discount on cash purchases.


Issues influencing
WORKING CAPITAL MANAGEMENT
Changing Market Conditions
Supply Chain Relationships
Competitive Actions
Regulatory Compliance