ASSIGNMENT - 10

Define Cash conversion cycle :-

The Cash conversion cycle (CCC) is a metric that measures that time (in days) it takes for a company to convert its instruments in inventory and other resources into Cash flows from sales. It reflects the efficiency with which a company manages its working Capital.. The CCC helps a company understanding how long each dollar invested in operations its tried up before it is converted into Cash.

The formula for the Cash conversion cycle is

CCC = Days Inventory outstanding (DIO) + Days sales outstanding (DSO) - Days payables outstanding (DPO)

Key Components :-

Day Inventory Outstanding (DIO) :-

The average number of days the company takes to turn its inventory into sales. A lower DIO indicates efficient inventory management.

$$DIO = \frac{\text{Average Inventory}}{\text{Cost of Good sold } [COGS]} \times 365.$$

Day Sales Outstanding (DSO) :-

The average number of days it takes the company to collect payment after making a sales. A lower DSO means the company is collecting payments from customers quickly.

$$DSO = \frac{\text{Accounts Receivable}}{\text{Total Credit Sales}} \times 365$$

Days payable outstanding (DPO) :-

The average number of days the company takes to pay its suppliers after receiving inventory. A higher DPO is generally better for cash follow as the company can hold onto its cash longer.

$$DPO = \frac{\text{Accounts payable}}{\text{COGS}} \times 365.$$