Assignment-11

Explain the determinants of working capital.

The determinants of working capital are factors that influence the amount of working capital a business needs to operate effectively. working capital; the difference between a company's current assets (such as cash, accounts receivable, and inventory) and its current liabilities (such as accounts payable and short-term debts). Several factors can affect the required level of working capital:

Nature of Business:

companies involved in manufacturing typically require more working capital due to large investments in rawmaterials and inventories, while service-based businesses might need less as they hold fewer inventories

Business cycle:

During expansion phases, businesses may need more working capital to meet rising production and sales, while during recessions the need may decrease as production slows down.

Production cycle:

Companies with longer production cycles require more working capital to cover the costs of labor, raw materials and overheads until goods are sold and cash is received.

Credit Policy:

If a company offer longer credit periods to customers, it will need more working capital to cover the delay in receiving payments. Conversely, if it can get favorable credit terms from suppliers, it may need less working capital.

Operating efficiency:

Firms that manage their inventory, accounts receivable and accounts payable efficiently can reduce the amount of working capital they require.

Market conditions:

In a competitive market, firms may need more working capital to finance promotions, discounts or maintain larger inventories to quickly meet customer demand.