**12th Week Assignment**

1. Should we include cash for a firm while calculating working capital? What are the common reasons for the inclusion or exclusion?

Inclusion: Including cash in working capital provides a more conservative estimate of a company's short-term liquidity. This is because cash is the most liquid asset, readily available to meet current obligations.

Exclusion: Some analysts exclude cash because it's argued that cash is not directly involved in the conversion cycle of turning raw materials into finished goods, selling those goods, and collecting cash from customers. They argue that focusing on current assets that are directly involved in the operating cycle provides a more focused measure of a company's ability to pay its short-term liabilities.

1. Given the data on two companies – Provogue and Kewal Kiran, which one do you think is better managed? Why?



Provogue vs. Kewal Kiran

Data Limitations

It's difficult to definitively say which company is better managed based solely on the data provided in the image. A more comprehensive financial analysis would be required to make such a judgment.

However, based on the data provided, Provogue appears to have an advantage in terms of working capital management.

Provogue has a higher percentage of receivables than Kewal Kiran across all the years. This could indicate that Provogue is more efficient in collecting payments from customers. Lower receivables tie up less cash, which can improve liquidity.

It appears that Provogue also has a lower inventory turnover (a higher percentage of inventory relative to sales) than Kewal Kiran in most years. While this could be a sign of inefficiency, it could also indicate that Provogue is holding more safety stock, which may be necessary due to the nature of its business or supply chain.

Further Analysis

A more comprehensive analysis would consider factors beyond those shown in the image, such as:

Gross profit margin: A higher margin indicates a company is more efficient at generating profit from its sales.

Current ratio: This ratio compares a company's current assets to its current liabilities. A higher ratio indicates a greater ability to meet short-term obligations.

Debt-to-equity ratio: This ratio measures a company's financial leverage. A lower ratio indicates a company is less reliant on debt financing, which can be a sign of financial stability.

1. Explain how significant jumps or dips in working capital may be a symptom of trouble for the firm.

Significant jumps or dips in working capital can be a red flag for potential trouble in a firm, for a few reasons:

1. Liquidity Issues:

Sudden Dip: A large decrease in working capital can indicate a shortage of cash to cover short-term liabilities. This could be due to:

Slowing sales and declining receivables (money owed by customers)

Increased inventory levels that tie up cash

Difficulty paying suppliers, leading to higher payables (money owed to suppliers)

Large cash outflows for unexpected expenses

Sudden Jump: While a jump might seem positive initially, it could also indicate inefficient use of cash. The firm might be:

Holding excessive inventory that isn't selling well

Granting overly generous credit terms to customers, leading to slow collections

2. Operational Inefficiency:

Large Fluctuations: Frequent and significant swings in working capital can suggest a lack of control over inventory management and credit policies.

High Working Capital: Consistently high working capital might indicate the firm is inefficiently converting inventory to sales or collecting payments from customers slowly. This ties up cash that could be used for more productive purposes.

Low Working Capital: Conversely, chronically low working capital can signal the firm is taking excessive risks. They might be:

Holding minimal inventory, leading to stockouts and lost sales

Offering very strict credit terms, which could limit sales opportunities

3. Underlying Problems:

Significant changes in working capital can sometimes be a symptom of deeper issues within the company, such as:

Declining sales or profitability

Supply chain disruptions

Management problems

However, it's important to consider the context:

Seasonal Businesses: Some industries have seasonal peaks and troughs. Working capital needs might naturally fluctuate throughout the year.

Growth Spurt: A rapidly growing company might see a temporary increase in working capital as they invest in inventory and receivables to support future sales.