

Assignment - 7

Define working capital

The amount needed to be ~~fund~~^{run} the day to day operation. working capital also known as net capital (NWC) is the difference between a company's current assets (like cash, accounts receivable/credit, unpaid bills and inventories of raw materials, finished goods and its current liabilities such as account payable and debts.

Understanding working capital.

Working capital is calculated from the assets and liabilities on a company's balance sheet, following on immediate debts and the most liquid assets.

Calculating working capital provides insight into a company's short-term liquidity and efficiency.

Working capital formula

$$\text{Working Capital} = \text{current asset} (-) \text{current liabilities}$$

Positive Vs negative working capital

⇒ This calculation is positive, it indicates that the company's current assets exceed its current liabilities.

⇒ This calculation is negative the company's current assets are insufficient to cover its current liabilities.

Components of working capital

- * Current Assets
- * current liabilities.

Current Assets

current assets are economic benefits that the company expects to receive within the next 12 months.

eg:-

Cash and cash equivalents, Inventory, Account Receivable, Note Receivable, Prepaid Expenses.

Current Liabilities

current liabilities encompass all debts a company owes or will owe within the next 12 months.

e.g:-

Accounts Payable, wages Payable, current Portion of Long term debt, Accrued tax Payable, Dividend Payable, unearned Revenue.

Limitations of working capital.

- * changing values
- * Nature of Assets
- * Assets Realization.
- * unknown debt.