

Assignment - 7

Define working Capital

Working Capital, also known as net working capital (NWC), is the difference between a company's current assets like cash, accounts receivable, customer's unpaid bills and inventories of raw materials and finished goods and its current liabilities such as accounts payable and debts.

Understanding working capital

Working Capital is calculated from the assets and liabilities on a corporate balance sheet focusing on immediate debt and the most liquid assets.

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

Working Capital Formula:

$$\text{Working Capital} = \text{Current Assets} - \text{Current Liabilities}$$

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 Asset

⇒ Current Liabilities.

Current Asset

Current Asset are economic benefits that the company expects to receive within the next 12 months

eg:-

cash and cash Equivalents inventory.
Account Receivable, notes Receivable,
Prepaid Expenses.

Current liabilities

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

eg:-

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 Devaluation.

* Unknown Debt.