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Applied Financial Statement Analysis

Assignment - 6 - 10

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Explain about Negative Working capital and in what Perspective It will be Good. Why?

Negative Working capital accures when a companys current liabilities exceed its current assets. In simple terms. it mean's that a company doesn't have enough sheet-term assets (like cash. receivables or inventory) to covers its short-term obligations (like Payables short-term loans. or accrued expenses) This can sound alarming but in some cases. it can actually be a sign of efficiency, depending on the business model.

When negative working capital can be Good:.

1. cash-flow Efficient Business.

companies with strong cash flow and low reliance on inventory can benefit from negative working capital for example. retail business (like supermarkets or online retailers) often receive cash from customers upfort but have time before they need to Pay supplies This means they don't need a lot of working capital and they may deliberately run with negative working capital.

Fast Turnover Industries:

Business with quick inventory turnover and short sales cycles, such as fast food chains a e-commerce Platforms can operate with negative working capital they receive Payments from customers quickly (sometimes before delivering goods) but supplies are Paid on credit terms, creating a situation where liabilities temporarily exceed assets.

supplier Financing:

companies may intentionally extend their Payment terms with suppliers, using this credit as a form of short-term financing. This enables them to Keep less cash or working capital on hand while still fulfilling operation. Essentially the business is using suppliers to finance operation rather than its own capital

Why Negative working capital can be beneficial:

Lower Financing Needs: companies with negative working capital don't need to raise or hold as much cash for operations, reducing borrowing or capital costs

Higher efficiency: It can reflect operational efficiency, especially in industries where goods are sold quickly and Payments are delayed to supplies

Focus on core activities: Firms can allocates their resources to more Productive areas (like expansion or innovation) instead of tying up cash in working.