ASSIGNMENT - 9

Why are we exlude cash while calculating working capital?

Cash is excluded while calculating working capital in certain cases (like operating working capital) to provide a more accurate view of the company's operational efficiency and liquidity. The main reasons include:

1. Cash is already liquid: Working capital measures how well a company can manage its current assets (like inventory or account receivable) to cover current liabilities. Since cash is immediately liquid and doesn't need conversion, it's often excluded to focus on assets that require more management.

2. Focus on operational assets: Operating working capital measures only those current assets and liabilities directly tied to daily operations (such as inventory and receivables). Cash, especially excess cash or reserves, may not be directly related to these operations.

3. Cash management can vary: Companies may hold large amount of cash for reasons unrelated to their operations, such as for future investments or to cushion against risks. Excluding cash offers a better reflection of how well a company is managing non-cash assets to meet short-term obligations.

However, not all definitions of working capital exclude cash. It depends, on whether the focus is on operating working capital or net working capital.