WORKING CAPITAL

Here's a summary of the key topics covered in the PDF, along with short notes:

1. Concept of Working Capital (Part-I)

- Working Capital Definition: The money invested in current assets (raw materials, finished goods, receivables).
- Necessity: Businesses need working capital to run smoothly, not just fixed assets.
- Example: A polythene bag manufacturing business illustrates how working capital is used.
- Net Working Capital: The portion of working capital funded by the company's own funds (capital or long-term borrowings).
- Total/Gross Working Capital: The total current assets, funded by short-term credit (including bank finance) and net working capital.

2. Working Capital Cycle (Part-I)

- Definition: The cycle of converting raw materials into finished goods, selling them, collecting cash, and purchasing raw materials again.
- Factors Affecting Cycle Length:
  - Raw material stock levels.
  - Work in progress duration.
  - Credit period given to customers.
- Importance: A longer cycle means a higher working capital requirement.

3. Methods for Calculating Working Capital (Part-II)

- Working Capital Definition: A firm's investment in current assets.
- Sources for Working Capital:
  - Own Sources (Net Working Capital).
  - Suppliers' Credit.
  - Other Current Liabilities.
  - Bank Finance.
- Permissible Bank Finance Methods (Tandon Committee):

- First Method: Requires the company to fund 25% of the working capital gap (Current Assets - Other Current Liabilities).
- Second Method: Requires the company to fund 25% of total current assets.
- Third Method: Requires the company to fund 100% of core current assets and 25% of the remaining current assets.

4. Turnover and Cash Budget Methods (Part-III)

- Turnover Method:
    - Suggested by the Nayak Committee.
    - Assumes working capital is 25% of annual turnover, with the bank providing 20% and the company 5%.
    - RBI guidelines for MSEs recommend working capital limits of 20% of annual turnover (up to Rs. 5 crore limit).
- Cash Budget Method:
    - Involves estimating cash inflows and outflows to determine working capital needs.
    - Used for seasonal industries or projects with fluctuating cash flows.

5. Drawing Power (Part-IV)

- Drawing Power (DP): The limit up to which a borrower can withdraw funds against the security of current assets (stock and debtors).
- Calculation:
    - DP = (Stock - Creditors) - Margin + (Debtors - Margin)
    - Margin is typically 25% (if not specified).
- Key Points:
    - Stock includes raw materials, work in progress, and finished goods.
    - Debtors are usually considered up to 90 days.
    - Drawing power is compared against the sanction limit.
    - Previous month's stock is used to calculate DP for the current month.

Let me know if you'd like a more detailed explanation of any of these points!