

Al-Saudia Virtual Academy Pakistan Online Tuition

WORKING CAPITAL

DEFINITION;

The term working capital is synonymously used with current assets. Working capital is an important ingredient of financial sources and management. Its excess or shortage may result in damaging consequences to the business, it is defined as an excess of current assets over current liabilities.

Example:

Working capital is the excess of current assets over current liabilities. In fact, working capital is the sum total of current assets including cash, merchandise inventory, receivables, and marketable securities. It can be explained in equation form as follows.

Working Capital = Current Assets - Current Liabilities

SOURCES OF WORKING CAPITAL;

Once the firm has considered the right source or source it may avail funds from the following types of short-term finance.

Trade accounts or trade credits (A/P)

1. Installment purchases (Hire purchase)
2. Commercial draft (Bill of exchange)
3. Accommodation bill.
4. Pledging accounts receivable/ Factors
5. Commercial paper (promissory note)
6. Overdraft
7. Agricultural banks
8. Call loans
9. I owe you (I owe you)
10. Two-name paper advance.

MEASURE OF WORKING CAPITAL;

Financial managers need to know the position of working capital to determine the company's liquid financial position. To measure the liquidity position the firm uses the following methods.

AMOUNT OF WORKING CAPITAL;

Working capital as discussed earlier, is the excess of current assets over current liabilities. The knowledge of the amount helps the firm know its abilities ability to pay off its debts and meet short-term cash requirements.

QUALITY OF WORKING CAPITAL;

Quality of working capital is also important to determine the ability of the firm to meet its short term requirement. Some merchandise is easily converted into cash while other items are slow-moving. Hence the quality determines how ready is the working capital to meet short-term needs.