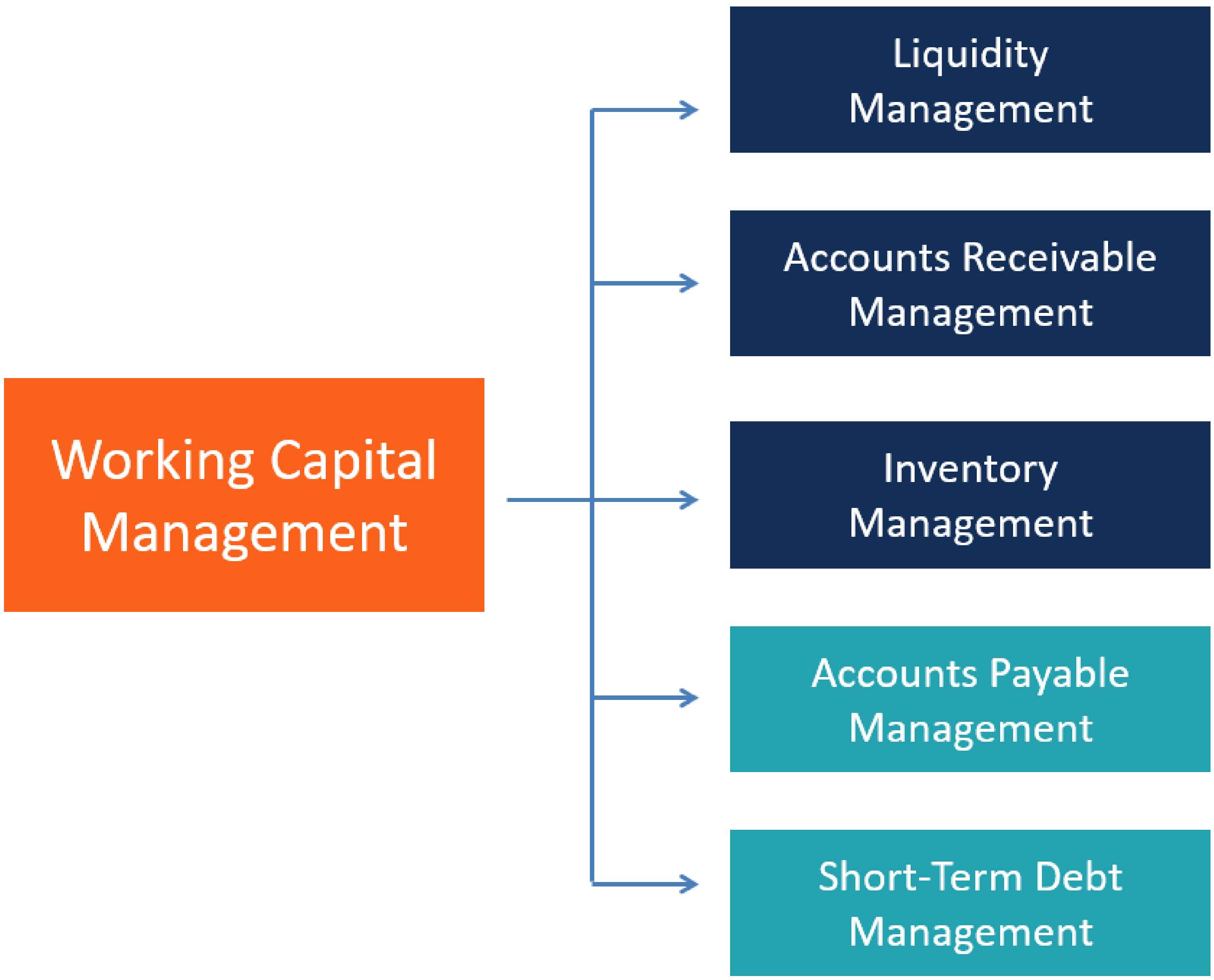
Part 5 : lecture 2

Working Capital Management

Working capital management refers to the set of activities performed by a company to make sure it got enough resources for day-to-day operating expenses while keeping resources invested in a productive way.



Understanding Working Capital

Working capital is the difference between a company's current assets and its current liabilities.

Why Working Capital Management is Important

Ensuring that the company possesses appropriate resources for its daily activities means protecting the company's existence and ensuring it can keep operating as a going concern. Scarce availability of cash, uncontrolled commercial credit policies, or limited access to short-term financing can lead to the need for restructuring, asset sales, and even liquidation of the company.

Factors That Affect Working Capital Needs

Working capital needs are not the same for every company. The factors that can affect working capital needs can be endogenous or exogenous.

Endogenous factors include a company's size, structure, and strategy.

Exogenous factors include the access and availability of banking services, level of interest rates, type of industry and products or services sold, macroeconomic conditions.

Managing Liquidity

Properly managing liquidity ensures that the company possesses enough cash resources for its ordinary business needs and unexpected needs of a reasonable amount. It's also important because it affects a company's creditworthiness, which can contribute to determining a business's success or failure.

The lower a company's liquidity, the more likely it is going to face financial distress, other conditions being equal.

Managing Accounts Receivables

A company should grant its customers the proper flexibility or level of commercial credit while making sure that the right amounts of cash flow in via operations.

Managing Inventory

Inventory management aims to make sure that the company keeps an adequate level of inventory to deal with ordinary operations and fluctuations in demand without investing too much capital in the asset.

Managing Short-Term Debt

Like liquidity management, managing short-term financing should also focus on making sure that the company possesses enough liquidity to finance short-term operations without taking on excessive risk.

Managing Accounts Payable

Accounts payable arises from trade credit granted by a company's suppliers, mostly as part of the normal operations. The right balance between early payments and commercial debt should be achieved.