



RAMA UNIVERSITY

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FACULTY OF COMMERCE AND MANAGEMENT

COURSE: MBA III SEM..

SUBJECT: WORKING CAPITAL MANAGEMENT

SUBJECT CODE: MBAFM02

LECTURE: 1

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LECTURE-1



WORKING CAPITAL MEANING

WORKING CAPITAL

Capital required for a business can be classified under two main categories

- (1) Fixed Capital
- (2) Working Capital

Every business needs funds for two purposes for its establishment and to carry out its day-to-day operations. Long-term funds are required to create production facilities through purchase of fixed assets such as plant and machinery, land, building, furniture etc. Investments in these assets represent that part of firm's capital which is blocked on a permanent or fixed basis and is called fixed capital. Funds are also needed for short-term purposes for the purchase of raw materials, payment of wages and other day-to-day expenses, etc. These funds are known as working capital.

Definition

In the words of Shubin, "Working capital is the amount of funds necessary to cover the cost of operating the enterprise".

According to Genestenberg, "Circulating capital means current assets of a company that are changed in the ordinary course of business from one form to another, as for example, from cash to inventories, inventories to receivables, receivables into cash".

CONCEPTS OF WORKING CAPITAL

There are two concepts of working capital:

- (A) Balance Sheet Concept
- (B) Operating Cycle or Circular Flow Concept

(A) Balance Sheet Concept: There are two interpretations of working capital under the balance sheet concept:

- (i) Gross Working Capital
- (ii) Net Working capital

In the broad sense, the term working capital refers to the gross working capital and represents the amount of funds invested in current assets. Thus, the gross working capital is the capital invested in total current assets of the enterprise; current assets are those assets which in the ordinary course of business can be converted into cash within a short period of normally one accounting year.

Examples of Current Assets are:

CONSTITUENTS OF CURRENT ASSETS	
1.	Cash in hand and bank balances.
2.	Bills Receivables.
3.	Sundry Debtors (less provision for bad debts.)
4.	Short-term loans and advances.
5.	Inventories of stocks, as:
	(a) Raw Materials,
	(b) Work-in-Process,
	(c) Stores and spares,
	(d) Finished Goods.
6.	Temporary Investments of surplus funds.
7.	Prepaid Expenses.
8.	Accrued Incomes.

In a narrow sense, the term working capital refers to the new working capital. Net working capital is the excess of current assets over current liabilities or say:

$$\text{Net Working Capital} = \text{Current Assets} - \text{Current Liabilities.}$$

Net Working Capital may be positive or negative. When the current assets exceed the current liabilities the working capital is positive and the negative working capital results when the current liabilities are more than the current assets. Current liabilities are those liabilities which are intended to be paid in the ordinary course of business within a short period of normally one accounting year out of the current assets or the income of the business.