Working capital

Finance

WORKING CAPITAL Presented by (Your school) Sure to focus on working capital, current ratio, short-term and long-term debt. End with a bulleted summary addressing the CFOs concerns as related to these areas. Superiors balance sheet.

Working capital Working capital mainly is concerned with the liquidity of operation of a company. It is considered as part of operating capital of a business or organization. Working capital of a firm or a business is calculated as the current asset minus the current liabilities of the balance sheet of a firm.

The balance sheet of superior shows a working capital of 33, 200 in 2001, 35, 400 in 2002 and 34, 750 in 2003. This shows a positive figure on the three balance sheets for superior. This means that the liquidity of the firm is positive and therefore, the firm is able to convert its asset to cash.

If the current asset of the firm was less than the current liabilities, this will mean that the firm has a deficit working capital and the firm will not be in a position to convert its asset into cash even if the company is making profits. (Livingstone 2002)

Hence this firm is in a chance to continue in its operation and be able to satisfy its short term debt and its operating expenses.

Current ratio

It is defined as the company’s ability to meet its short term obligations. These means that the higher the ratio the more liquid is the firm. The current ratio of a firm is calculated as a current asset divided by the current liabilities, the interpretation on these is that if the current asset of a firm is twice the current liabilities, then the firm is considered to have a significant good short term financial strength. But if the firm’s current asset are less

than the current liabilities of the firm, then the result will be a firm having a problem in meeting its short term financial problem.

Therefore, looking at the balance sheet of superior company the current ratio is as follows 1. 97 in 2001, 1. 95 in 2002, 1. 83 in 2003 these shows that the company is in a position of meeting its short term financial obligation for the ratio is a positive figure and the current asset are approximately twice the current liabilities.

Short term debt

These are short term loan and have a short maturity usually one year or less, in the balance sheet these amounts are indicated along the current liabilities section. They are mainly due within a year, if a company has more short term debt than the cash or investment to cover the bed payment then the firm will be forced to apply for more debt and this will be disadvantageous for the firm financially. (Droms 1990)

Based on the presented balance sheet of superior company its short term debts are 1, 200 in 2001, 1, 300 2002 and 1, 450 in 2003. Meaning therefore, the firms short term debt are less than the cash of the company and hence, the company has no intention of acquiring more debt for it is able to finance for the debt it has.

Long term debt

These are debt that are payable for more than one year, they do include bank loan, debentures, mortgage bonds that are to be paid for more than a year. The long term debts are found in the balance sheet on the long term liabilities section. A firm must on all occasion disclose the long term debt in its balance sheet for it is used to measure a firm's financial leverage.

A firm will use the long term debt ratio to calculate for the financial leverage

which is calculated by dividing the long term debt by the available capital. (Dembinski 2006)

Advice to the Chief Financial Officer (CFO) on the concerns of superior balance sheet

Under the working capital shown above, it means that the firm is in a able to convene its financial obligation, and the CFO of the company should advice the management that the firm performing healthy, and it should also continue working at the same level or increase its working capital to put in a better position to meet its financial obligations.

Under the current ratio of the company, the ratio shows an approximate value of 1. 97, 1. 95 and 1. 83. This is a clear indication that the firm is in a good situation to cater for its short term financial obligation, but this is not a particularly favourable good situation for the business for it need to have a current ratio of 2 and above to give it a strong position.

Under the short term debt of the company, it is in a position to pay for its short term debt for the debt is small than the cash or the investment of the company. So the CFO should encourage the firm to continue operating at the same level.

Under the long term debt of the company as indicated by the balance sheet, the financial leverage of the company is constant thus the CFO should continue operating at the same level and the business will be save and will operate a profit.

References

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