

# [The firms operating cycle and its cash conversion cycle essay sample](https://assignbuster.com/the-firms-operating-cycle-and-its-cash-conversion-cycle-essay-sample/)

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Any firm should pay attention to its inflows and outflows of the cash in order not to become a bankrupt. Thus, focusing on operating cycle and cash conversion cycle, which include all cash flows in and out of the firm, its financial situation can be easily estimated.
Regarding operating cycle, it is the period of time from the moment the firm spends money to buy raw materials till it receives money from sales of products (Baker, p. 163). Also, it includes the duration of work-in-process and finished goods and time needed to sale these products. As for the cash conversion cycle, it is the period of time when the firm ties up its money in current assets (Bose, p. 14). In other words, it is the time between receiving cash from the product sales of the firm and expending this cash on materials and labor.
The main difference between these two cycles is that during the calculation of the cash conversion cycle the firm determines the payment deferral period, meaning the period when the firm buys raw materials on credit and makes the cash payment for the expenses (Baker, p. 164). That is why the operating cycle is usually longer than cash conversion cycle.
Both of the cycles are very important for the firm to prosper, but still, to my mind, the operating cycle is more essential. The reason for this is that it shows the whole operating management performance of the firm and the best situation is when the cycle is shorter. The cash conversion cycle focuses only on the duration of the time when the financial flows are engaged in this cycle, but it does not pay any attention to funds committed to a product moving through it.

## Works Cited

Bose, Chandra D. Inventory Management. New Delhi: Prentice-Hall of India Private Ltd, 2006. Print.
Baker, H. Kent, and Gary E. Powell. Understanding Financial Management. Carlton: Blackwell Publishing Ltd, 2005. Print.