



**Universidad del Desarrollo**  
Universidad de Excelencia

# **Finance I**

## **Fall 2012**

### **Session 17:**

# **Working Capital Management**



**1. Recap**

**2. Working Capital Management**

**3. Closing**

- ▶ **What are the most commonly used financial statements?**
  
- ▶ **Ratios can be constructed to analyze de financial and operational information of a company, typically in 4 main areas:**
  - Financial condition (Debt)
  - Liquidity
  - Efficiency
  - Profitability
  - Book mentions a fifth, regarding Market value (only for traded companies)
  
- ▶ **What is the DuPont System?**

**1. Recap**

**2. Working Capital Management**

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## 2. Working Capital

- ▶ **The amount of money required to keep the company running on a daily basis**
- ▶ **Usually referred as the sum of current assets and current liabilities**
- ▶ **If current liabilities are larger than current assets, the company:**
  - Generates funds?
  - Requires additional funds?

## 2. Working Capital

- ▶ **Remember that assets are what the company owns. The company paid for them.**
- ▶ **The liabilities are what the company owes. The company received money and owes it.**
- ▶ **Then, if the current liabilities are larger than the current assets, it means that on a day to day basis, the company receives more money than it uses in the short term**
- ▶ **In general, a company wants to have little amounts of current assets and larger amounts of current liabilities**

## 2. Working Capital

### ▶ Current Assets:

- **Cash and equivalents**
- Inventories
  - Finished products
  - Products in process
  - Raw materials
- Accounts receivables
- Other Current Assets

### ▶ Current Liabilities:

- Short term loans
- Accounts payable
- Accrued income tax
- Current payments of long term debt
- Other current liabilities

# 2. Working Capital Current Assets' Management

- ▶ **General rule: as little as required**
  
- ▶ **Cash: depending of immediate short term payments**
  
- ▶ **Inventories: depending on economic order quantity (EOQ)**
  - Larger the order, cheaper the unit cost (discounts, transport, handling, etc.)
  - Larger the order, higher the carrying cost (storage, insurance, theft, cost of capital)
  - There is a minimum total cost => EOQ



## ▶ Account Receivables:

- Depends on credit policy. No credit => No account receivables
- Credit policy is not only a financial decision. Includes a business plan approach.
- The book simplifies the approach using a discounted cash flow on the probabilities of payment
  - Probability of payment and probability of default
  - Earnings of payment and losses of default

1. Recap
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## 2. Working Capital

- ▶ **What is working capital?**
  
- ▶ **If current liabilities are larger than current assets, the company:**
  - Generates funds?
  - Requires additional funds?
  
- ▶ **If you are the owner of a company, would you rather have positive (assets>liabilities) or negative (liabilities>assets) working capital**
  
- ▶ **If a company is growing, would you rather have positive (assets>liabilities) or negative (liabilities>assets) working capital**

## ▶ Next week Wednesday:

- TA Session
- Recap of all contents
- Propose questions for the midterm!!!
- Quiz 5
- Videos will be posted on Wednesday

## ▶ Midterm based on 10, 18, 29 and 30

- Saturday 26 at 10:00 at room 307
- Bring calculator. Cellphones and sharing calculators will not be allowed