

Meaning and Significance of Working Capital

In every business there is a permanent existence of two types of assets: One is fixed asset and other is current asset. Fixed asset include those assets which are not required for resale or not being consumed in production but are to be kept permanently for for a long term in business such as land and building, plant and machinery, furniture and Fittings etc. The nature of such assets is either permanent or long term. On the contrary, Current assets are of short-term nature and are meant either for resale or being consumed in production process such as cash, current investment, inventory, receivables etc. Current assets circulate along with business operation and hence they are also called circulating assets. The part of firm's capital that is used to finance the short term assets or current assets is called working capital. It is also known as circulating or revolving capital.

Thus, working capital refers to the fund which we need for short term purposes such as purchase of raw material, payment of day to day expenditures or operating expenses of the business. These funds are known as working capital. In this way, we find that working capital is that part of capital which is used in financing the current assets and meeting the operating cost of the organisation where the duration of the financing is maximum 1 year. Thus, working capital has two concepts, one is gross concept and other is net concept. Gross concept of working capital represents the capital involved in total current assets and net concept of working capital represent the excess of current assets over current liabilities. The gross working capital is a financial concept where as the net working capital is an accounting concept. In financial management, we consider the net concept of working capital. so far the significance or importance of working capital is concerned, we find that working capital seems to be the life blood and nerve centre of any business. Working capital ensures smooth functioning of any business enterprise. working capital is very essential to run the business smoothly, without an adequate amount of working capital no business can run successfully. The main advantages of maintaining adequate amount of working capital are as follows:

(1) Solvency of the business :It helps in maintaining solvency of the business by providing uninterrupted flow of production.

(2) Helpful in maintaining Goodwill : It enables the business concern to make prompt payment and hence helps in creating and maintaining goodwill.

(3) Easy loans: A concern having adequate working capital, high solvency and good credit standing can arrange loans from banks and others at an easy and favourable terms and conditions.

(4) Cash discounts: The availability of the working capital goes to ensure the business firm in availing the cash discount at the time of purchasing the raw material and other things therefore reduces the cost of the organisation.

(5) Regular supply of raw materials: The availability of the working capital goes to ensure the regular supply of raw materials and continuous production.

(6)Regular payment of salaries ,wages and other day-to-day commitments: The availability of the working capital goes to ensure the concern for making payment of salaries, wages and other day today commitment on regular basis or on the date of maturity .This availability of the working capital goes to raise the morale of its employees, increases their efficiency, reduces wastages and costs and hence, enhances production and profits.

(7)Exploitation of favorable market condition: The availability of the working capital can exploit favorable market conditions such as purchasing its requirements in bulk when the prices are lower and by holding its inventory for higher prices.

(8) Ability to face crisis: Sufficient working capital enables a concern to face business crisis in emergencies such as depression, recession because during such Period there is much pressure on working capital.

(9)Quick and regular return on investments: sufficient of working capital enables a concern to pay quick and regular dividend to its investors. This goes to improve the confidence of its investors and create a favorable market to raise additional funds in future which is of great help for any business enterprise.

(10)High morale: Adequacy of working capital creates an investment of security, confidence, high morale and creates overall efficiency in a business.

Thus, we find that working capital is going to be very beneficial for any business enterprise because the availability of the working capital goes to strengthen the financial position of business enterprise .It goes to provide the base for its solvency and making the different commitments in time .It goes to improve the goodwill and reputation of any business enterprise. The ability of raising loan for a any business enterprise is also going to be increased with the availability of the working capital in any business .In this way, we find that the availability of the working capital goes to ensure the stability of any business enterprise during the period.