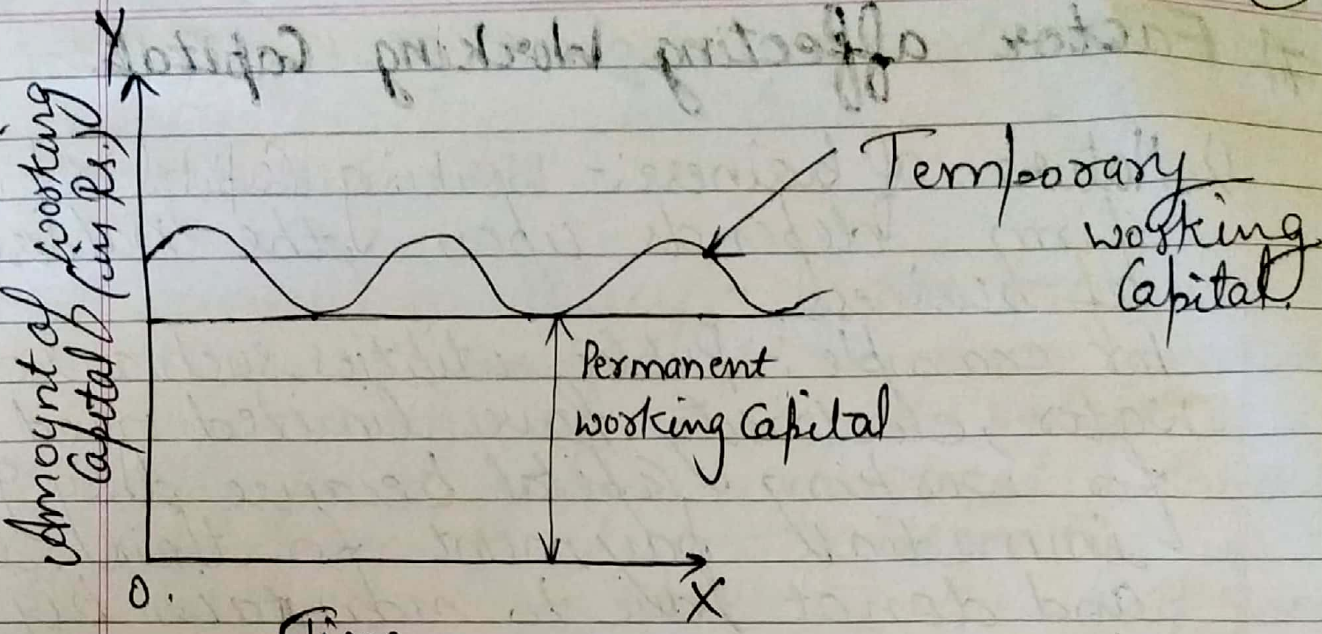
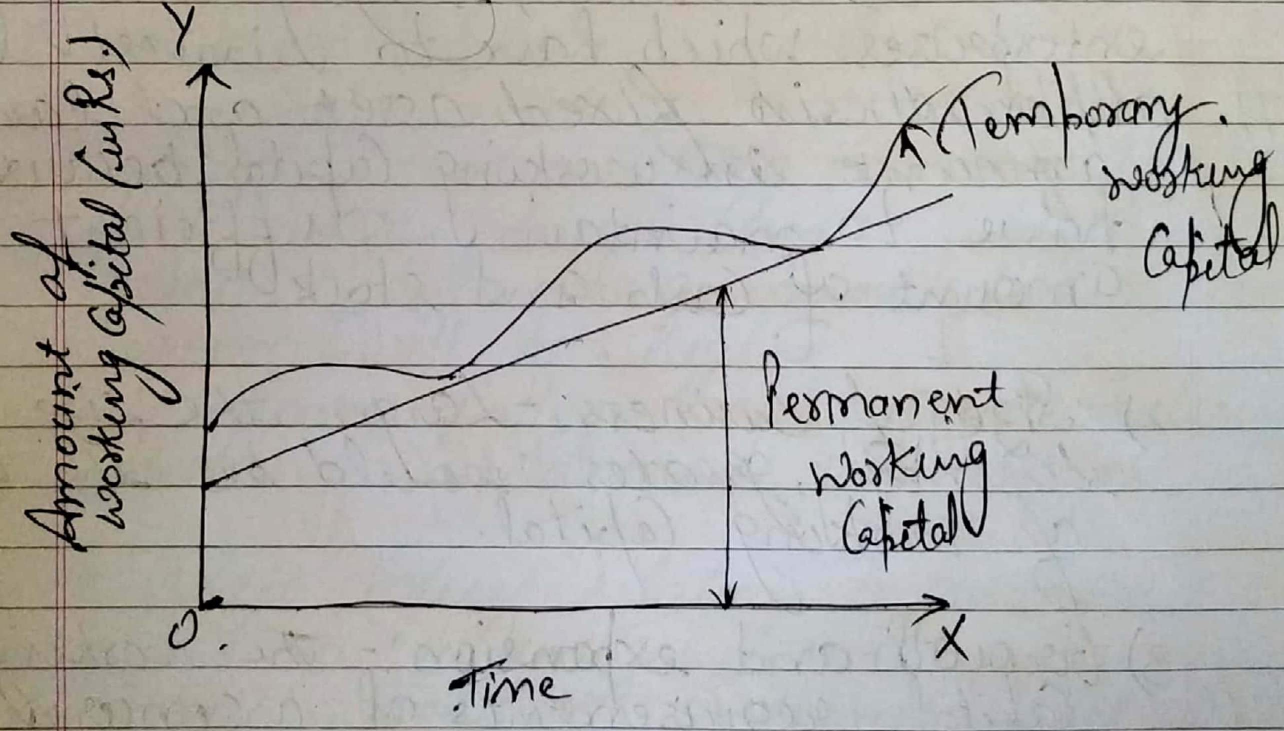


Fig(1)



Fig(2)

Fig(1) Shows that permanent working capital is stable while temporary working capital is fluctuating.

Fig(2) In case of expanding concerns, the need for permanent working capital may not be constant & it would be increasing.

Factor affecting Working Capital

1) Nature of business:- Working Capital of the firm depends upon the nature of business.
for example:- Public utilities such as railway, water, electricity have limited need for working capital because they get immediate payment for their services and donot have to maintain big inventories.
on the other hand, trading and financial enterprises which have to invest less amount in fixed asset and large amount in working capital because they have to maintain sufficient amount of cash and stock.

2) Size of business:- Larger the size of business, greater would be the need of working capital.

3) Growth and expansion:- The working capital requirements of a concern increase with the growth and expansion of its business activities.

4) Business Fluctuations:- During boom period, the need for working capital increase because firm will have to operate at full capacity to meet increased demand.

In Dearing depression, the need for working Capital will be less because of low demand.

5). Production Policy:- If the product is seasonal, Then it is to be produced in months of demand only or the good may be produced throughout the year. If second alternative is adopted, then stock of finished goods will accumulate upto season of demand which require increasing amount of working Capital.

6) Credit Policy relating to Sales:- If the firm adopts liberal credit policy in respect of Sales, the amount tied up in debtor will be higher.
If firm follow tight credit policy, working capital need will decrease

7) Credit Policy relating to purchase:-
If firm purchase more goods on credit, need of working Capital will be less.

8) Dividend Policy:- If the firm does not pay dividend but retain the profit then its ~~need~~ main contribution will be towards working Capital.

Advantages of adequate Working Capital

* Availability of raw materials regularly
* Cash Discount
* Full utilisation of fixed assets.
* facility in obtaining bank loans.
* Meeting unseen contingencies.

Approaches to determine Working capital finance mix

- The hedging or Matching Approach
- The conservative Approach
- The aggressive Approach

(A) Matching Approach :- According to this approach, expected life of asset will be matched with expected life of source of funds raised to finance such asset. when firm follow matching approach,

✓ Permanent working capital need should be financed with funds from long term sources.

- Temporary working Capital should be financed through short term funds.

(B) Conservative Approach:-
According to this approach, all financial need of firm are financed through long term funds. Short term funds should be used only in emergency situation.

(C) Aggressive Approach:-
This approach suggest that entire estimated requirement of current asset should be financed through short term sources and even a part of fixed asset investment should be financed through short term sources.