**Working Capital - Example**

Equally important as

* maintaining optimal balance between equity and debt capital,
* is also maintaining optimal balance between long-term and short-term sources (source structure) of long-term and short-term capital (especially of long-term and short-term debt capital).

Short-term debt capital is cheaper than long-term debt capital.

**Short-term debt capital** should be used only for financing **liquid assets**, these are mainly money, debts due, or finished products, i.e. assets which can be used to repay these short-term debts (short-term debt capital) quickly and without loss.

**Long-Term Capital** (Long-term Debt and Equity) should cover **Fixed Assets** and permanently locked-up Current Assets.

* Using long-term debt capital for financing short-term assets is **inefficient**.
* Using short-term debt capital for financing fixed assets, in turn, carries a **high risk**.

Surplus of Current Assets over Short-term Debt (current liabilities) is called **Net Working Capital** – NWC. It can also be defined as the part of current assets being financed by long-term sources. Net Working Capital represents the amount of free resources available to the company after all current liabilities had been settled. It is desirable that it be kept directly in the form of money. A satisfactory amount of Net Working Capital is one of the signs of a good financial situation of the company.

If Short-term Debt becomes higher than Current Assets – which is utterly undesirable, a so-called **Flowing Debt** ensues.

**EXAMPLE to practice:**

Assess the relationships between the asset structure and the capital structure of the company on the basis of the balance sheet data (in thous. CZK).

|  |  |  |  |
| --- | --- | --- | --- |
| Assets BALANCE SHEET Liabilities | | | |
| Fixed Assets (in ZC) | 290 000 | Registered Capital | 260 000 |
| Inventory | 250 000 | Funds from earnings | 30 000 |
| Receivables | 110 000 | Profit – previous years | 150 000 |
| Cash and bank accounts | 150 000 | Long-term Payables | 140 000 |
|  |  | Short-term Payables | 220 000 |
| Assets Total | 800 000 | Liabilities Total | 800 000 |