

Paul Robbins training and consultancy

Credit Management

Working Capital Cycle

Exercise 1 **Model Answer**

You have been provided with the following extract from the latest Financial Statements of Bishopstone Ltd.

Statement of Profit or Loss (Extract)		
	£	£
Sales		328,000
Less Cost of Sales		
Opening Inventory	24,000	
Purchases	191,000	
	215,000	
Closing Inventory	(29,000)	
		186,000
Gross Profit		142,000

Statement of Financial Position (Extract)		
	£	£
Current Assets		
Inventory	29,000	
Trade Receivables	28,000	
Cash	11,000	
		68,000
Current Liabilities		
Trade Payables		24,000

You should calculate the Inventory Holding Period, Accounts Receivable Collection Period and Accounts Payable Payment Period ratios and use your answers to calculate the working capital cycle.

Note that all sales and purchases are made on credit and that you should use the closing inventory value to calculate the Inventory Holding Period ratio.

You should express your answers to the nearest whole day.

Inventory Holding Period

$$= (\text{Inventory} / \text{Cost of Sales}) \times 365$$

$$= (£29,000 / £186,000) \times 365$$

$$= 57 \text{ days}$$

Accounts Receivable Collection Period

$$= (\text{Trade Receivables} / \text{Sales}) \times 365$$

$$= (£28,000 / £328,000) \times 365$$

$$= 31 \text{ days}$$

Accounts Payable Payment Period

$$= (\text{Trade Payables} / \text{Cost of Sales}) \times 365$$

$$= (£24,000 / £186,000) \times 365$$

$$= 47 \text{ days}$$

Working Capital Cycle

$$= \text{Inventory Holding Period} + \text{Accounts Receivable Collection Period} - \text{Accounts Payable Payment Period}$$

$$= 57 \text{ days} + 31 \text{ days} - 47 \text{ days}$$

$$= 41 \text{ days}$$