

Working Capital Management - GCCFM 22

Project

You are the financial manager of CompanyC, a wholesaler.
Please solve following 3 business problems (use Excel whenever possible).

A.

To increase sales from their present annual 10 million €, CompanyC wants to try more liberal credit standards. Currently, the firm has an average collection period of 30 days. It's believe is that, with increasingly liberal credit standards, the following will result:

| Credit Policy | | A | B | C | D |
|---|------|----------|----------|----------|----------|
| Increased sales from previous level | M€ | 2.7 | 1.9 | 1.0 | 0.6 |
| Average collection period for incremental sales | days | 45 | 60 | 95 | 120 |
| Bad-debt on incremental sales | % | 1 | 3 | 5 | 8 |
| Average price of the products | € | 20 | | | |
| Average variable costs | € | 18 | | | |
| Pre-taxes opportunity costs | % | 20 | | | |
| Days per year | days | 360 | | | |

Which policy would be the best?
Has the original turnover any influence on your decision?

B.

CompanyC sells 5,000 pieces of ProductP per month and is trying to determine how many ProductP to keep in inventory. You have determined that it costs 200€ to place and settle an order. The cost of holding inventory is 4 €cents per month per ProductP in inventory. A 5-day lead time is required for delivery of the ordered ProductP.

- Develop the algebraic expression for determining the total cost of holding and ordering inventory.
- Plot the total holding costs and the total ordering costs on a graph where the horizontal axis represents size of order and the vertical axis represents costs.
- Determine the EOQ from the graph and by calculation.
- Bonus question: calculate the optimum using Excel's "solver"¹ function.

¹ "Solver" is a more complex function than "Goal seek". Maybe you have to install the add-in.

More information:

<http://office.microsoft.com/en-us/excel-help/about-solver-HP005198368.aspx?CTT=1>
<http://office.microsoft.com/en-us/excel-help/load-the-solver-add-in-HP001127725.aspx?CTT=1>
<http://office.microsoft.com/en-us/excel-help/results.aspx?qu=solver&origin=HA001111864>

or google "solver excel"

C.

CompanyC has a 1 million € revolving credit agreement with BankB. Being a favored customer, the rate is set at 1 % over the bank's cost of funds.

The Bank's cost of funds is expected to be 4 % for the coming year.

In addition, there is a 0.5% commitment fee on the unused portion of the revolving credit.

- a. If CompanyC expects to utilize, on average, 60% of the total commitment, what is the expected annual euro cost of the credit arrangement?
- b. What is the equivalent percentage cost when both the interest rate and the commitment fee are considered?
- c. What is the equivalent percentage cost if, on average, only 20% of the total commitment is utilized?
- d. If another bank is offering a loan for a fixed interest rate of 6% without any commitment fee, when is this offer favorable?