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MANU	CONVERSATION BETWEEN MANU AND VINU **ABOUT** **CURRENT RATIO**	VINU
		

Manu	Vinu! You are looking very angry. What happened?
Vinu	Manu! I am sick of our Bankers! They denied working capital loan to our company by just quoting one ratio.
Manu	What was that Vinu?
Vinu	They said our current ratio is very low and so they are not interested in funding our company.
Manu	Ohhh…..
Vinu	How can they talk like that? That too just by looking at single ratios? Unfair!!!!
Manu	Vinu! Don’t blame the bankers. They are just agents of public. If they are quoting a particular ratio as the main reason to deny the loan, then it sounds very serious. i.e., your company has to work on certain things very seriously now.
Vinu	Our company has long years of experience and presence in the market. I don’t see any problem with our company.
Manu	No Vinu! If Banker is not happy with your financial ratio, then your company should seriously work on it. Because, all most all the companies in the country or for that matter, in the world, works predominantly with Bankers funds. So, if a Banker is not satisfied with your financial ratios, then you have not equipped to the expectation of the major stake holder. This will affect the future direction of the company. You may not get timely fund and you may not be able to grow!!
Vinu	I agree Manu!
Manu	Moreover, bank funds are supposed to be the cheapest funds in view of its tax benefits. So you have to work on it.
Vinu	Ok! Tell me where we should work on?
Manu	First tell me that ratio, which bankers are not comfortable with.
Vinu	It is our Current Ratio of 0.87.
Manu	My Goddd…..I fully support that banker.
Vinu	Why????
Manu	You are in a Financial mess now. How can you expect a banker to support you at this stage?
Vinu	Can you explain clearly?
Manu	Vinu. Your current ratio is 0.87
Vinu	Yes
Manu	It is at its dangerous level. Do you know how current ratio is calculated?
Vinu	Yes! Very simple

	Current Ratio = Current Asset / Current Liability
Manu	Yes! Calculation is very simple. But implications are very serious.
Vinu	What’s wrong with our ratio?
Manu	Your ratio is 0.87 It means, -for every Re.1 of Current Liability (short term liabilities), -you have Re.0.87 of Current Assets (short term resource)
Vinu	What’s problem in that?
Manu	It is the problem. Your liability is Re.1 and for paying that liability you have only Re.0.87 with you. On the face, you don’t have sufficient money to pay even Re.1 fully. You are short by Re.0.13. Then how you will be able to pay the banker in Crores. This ratio says, you have borrowed more and you don’t have adequate cash resources to pay back. This also would mean, some short term creditors are angry with you, because you don’t have adequate cash, and so they may file case against your company for non payment! This may go even go up to liquidation of company through court order!
Vinu	My Goddd……..Is it so serious? So do you mean to say, we should have current assets matching current liability?
Manu	If you have current assets = current liability, your current ratio will be 1:1. But still banker will not be happy
Vinu	But why?
Manu	Because, sometimes, certain current assets will not be available for paying of your liabilities immediately
Vinu	Like?
Manu	Like Inventory, delayed debtors, etc.
Vinu	So?
Manu	So, banker will be expecting you to have more current assets. It means, you will have more resources to pay off your liabilities.
Vinu	Ok!

Manu	Only when you have more resources and less liabilities, your liquidity position is said to be comfortable!
Vinu	Yes! Now I understand, why our current ratio is very low? We purchased all most all our products on credit. So we had high level of Creditors. This had inflated the current liability. Since we purchased everything on credit, we had surplus cash, which we have invested in fixed assets which will take some more time break even and come back to us through profits.
Manu	Since you have converted your cash into fixed assets, your current asset level also have come down. On one side, your current liabilities have gone up and on the other side, your current assets have come down. Lower numerator and higher denominator has resulted in very low ratio for your company.
Vinu	Yes Manu!
Manu	It means, your company should be facing difficulty in making payments like salary, creditors, is it not?
Vinu	Yes Manu ☹
Manu	It is because, you have sourced lot of short funds (creditors) and in turn used them for long term purposes. You cash got locked in Fixed Assets which will not come back to you in short cycle. But your creditors will start asking for payments. So whatever cash realised will go to them and eventually it will affect even the salary payment.
Vinu	True!
Manu	These are the very common implications of lower current ratio which that banker had identified just looking at the number of 0.87. If the ratio is less than 1.00, we can presume all the above.
Vinu	So, how a current ratio should be?
Manu	Current asset should be greater than current liabilities. Theoretically, 2:1 is considered as ideal current ratio. But Banker will be happy, if your current ratio is at least 1.33
Vinu	What is that 1.33?
Manu	It means, for Every Re.1 of Current Liability, you should have Re.1.33 of Current Assets!
Vinu	I understood that! But what's special in that?
Manu	You calculate the proportion of current liability to current assets at that level
Vinu	Current liability – 1.00

	Current assets – 1.33 Current liability (1/1.33) is 75% of Current Assets.
Manu	Yes! Exactly. At current ratio of 1.33, you are funding 75% of current assets through current liability. It automatically conveys something else.
Vinu	Hmmm?? Remaining 25%?
Manu	Yes! It means remaining 25% is funded by ……….
Vinu	By???
Manu	What is known as 'NETWORKING CAPITAL'
Vinu	Yes. Current Assets – Current Liability = Net Working Capital
Manu	True! So when your ratio is 1.33, it means, you are contributing 25% to your business through Net Working Capital and it is the least expectation of any banker. i.e., Bankers are ready to fund 75% for Working Capital, provided Owner contributes at least 25% of funds and it is demonstrated through 1.33.
Vinu	Great….and Thank you Manu! I never thought Current ratio will convey so many things! Thanks again.
Manu	Welcome Vinu!

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Coverage:

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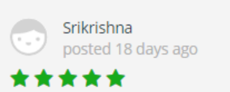
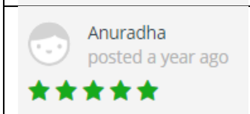
Section 2 - Financial Statement Reading Skills	Section 13 - Project Viability
Section 3 - Analysis of Financial Ratios	Section 14 - Cost of Project
Section 4 - Fund Flow Analysis for finding diversion of funds	Section 15 - Break Even Analysis
Section 5 - Cash Flow Analysis for understanding Cash Generation and Movement	Section 16 - Credit Rating
Section 6 - Types of Business Loans	Section 17 - CMA
Section 7 - Working Capital	Section 18 - Computerised Accounting System
Section 8 - Cash Credit	Section 19 - Banking Operations
Section 9 - Letter of Credit	Section 20 - Operational Aspects of KYC
Section 10 - Bank Guarantee	Section 21 - Loan Accounts
Section 11 - Project Report	Section 22 - Why Bankers do this do that Blah..Blah..Blah...

Best Reviews received for this course:

	Excellent
	Hii, first i took this credit analysis course..found it to be very good in understanding the concepts ...then i enrolled for many of Mr.Raja s courses after finding content is very good...explanation is also good.

SIDDHARTH YADAV posted 2 years ago	THIS IS BEST LECTURE EXPLAINED IN SIMPLE METHOD WITH EXAMPLES FOR CREDIT PROFESSIONAL. Also it would def help on the job purpose as well.Would def recommend