

Q1 ⇒) What factors determine the size of the Investment of a company in account receivable?

⇒) The size of Investment in receivable is Influenced by number of factors. Among them two factors, the Volume of credit sales, and the average length of time between sales and collection are important.

To illustrate suppose National Enterprise, a newly established firm makes a credit sales of \$ 5000 per day and its customers are allowed 15 days of credit. At the start of business i.e. In the first day, it sold \$ 5000 on credit so that its end-of-day account receivable stand \$ 5000 in the firm's book. During the second day, it sold another \$ 5000 on credit increasing the

book receivable do \$10,000. It is
 goes on granting a credit of
 \$5000 per day for 15 days,
 its account receivable will increase
 to \$75,000 at the end of 15th
 day. However in 16th day it will make
 another \$5000 credit sales, but
 payment for sales made on first
 day will reduce receivable by
 \$5000, so that total account receive-
 ble will remain constant at \$75000
 in 16th day and the each day thereafter
 throughout the year. The average
 account receivable the firm must
 carry during the year is therefore
 \$75000.

$$\begin{aligned}
 \text{Account receivable} &= \text{credit sales per} \\
 &\quad \text{day} \times \text{average} \\
 &\quad \text{length of collection} \\
 &\quad \text{period.} \\
 &= \$5000 \times 15 \text{ days} = \$75000.
 \end{aligned}$$