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Supported by:

How to Prepare a Cash Flow Forecast

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How to Prepare a Cash Flow Forecast

A cash flow is a forecast of when you expect to receive cash from your sales and when you expect to pay your bills. It is not and should not be confused with a proforma income statement. A cash flow is not an estimate of your sales and expenses; rather it is an estimate of when the money associated with sales, etc. will be received and when the money paying the expenses will be paid out.

WHY DO A CASH FLOW?

Too often business owners do a cash flow in their head. Putting the information down on paper will give you the following:

1. A format for planning the most effective use of your cash (cash management).
2. A schedule of anticipated cash receipts – follow through to see that you achieve it!
3. A schedule for priorities for the payment of accounts – stick to it!
4. A measure of the significance of unexpected changes in circumstances, i.e. reduction of sales, strikes, tight money situations, etc.
5. A list, on paper, of all your bill paying details and commitments, so that you can plan in advance to make sure you have the money to cover them.
6. An estimate of the amount of money you need to borrow in order to finance your day-to-day operations. This is perhaps the most important aspect of the completed cash flow projection.
7. An outline to show a potential lender that you will have the money necessary to make any scheduled loan payments if you are planning to borrow money on a term basis.

HOW OFTEN?

Cash flow planning should be a continuous activity, although it must be completely redone at least once a year for you to have a clear picture of additional cash requirements as most lines of credit are renewed annually. The cash flow will assist you in making an effective presentation to your lender.

Don’t put the cash flow away and forget it. For example, if you don’t meet your sales objective you have a sudden unexpected payment to make, take the cash flow out and work through it again. You will be able to see the effect of the change on your cash position and can logically illustrate any revised loan requirements to your lender.

Effective cash management is essential to survival and increased profits. Don’t leave cash inflow and outflow to luck and pressure. YOU WILL LOSE.

WHERE TO START

The first step in preparing a cash flow is to estimate sales on a monthly basis. Sales from previous years can be used to forecast sales for the coming year. If the business is new, there are a number of yard sticks that can be used to estimate sales. A relatively low or conservative forecast can be used to determine financial results of bad times. An optimistic forecast can be used to show the strain on working capital which may result from better than expected operations. Finally the most probable forecast between these two remains the anchor point about which plans are made.

When preparing a cash flow the purpose is to forecast cash receipts, to schedule payment and to forecast the use of operating funds (lines of credit) when necessary from the bank. The cash flow forecast illustrates the need and timing for money. It also illustrates when cash receipts will reduce or eliminate that need.

Estimate what amount of your sales will be cash and what amount will be credit. If last years sales were 20% cash and 80% credit and you do not plan to change your credit policies, chances are that the same proportions will occur again this year. If you sell on credit take into account when you can expect to collect the accounts receivable. For example, 60% within 30 days, 30% within 60 days, etc.

The next step is to plan for accounts payable on a monthly basis according to your sales projections. For example, if you pay your invoices on a 30 day basis, then the cash expenditures for January's purchases and expenses will be made in February. If you can obtain credit for longer terms, then cash outlays can be further delayed.

CASH FLOW WORK SHEET

Now that total cash collections and total cash payments on goods purchased have been estimated, use the cash flow work sheet to list all cash transactions for the month. Remember, only list the actual cash you are expecting to receive or spend in the appropriate monthly column. An explanation of some of the entries is given below.

Loan Receipts: If you take possession of borrowed money during that month, list the entire amount as a cash receipt in that month.

Operating Expenses: Enter the amount of your monthly expenses. This is actual cash outlay for the month. For example, if you write a cheque in January for the full year's insurance then the amount of the cheque would be put in the January column and nothing would be entered for the rest for the year.

Asset Purchases: If money is spent for the purchase of fixed assets such as a vehicle or filing cabinet, list the amount in the month when the cheque is written, not in the month when you take possession of the asset.

Loan Payments: Indicate the monthly payment for both the principal and interest on all loans both existing and anticipated.

Income Tax Payments: List the amount you expect to pay in income tax based on your business profits. You may want to remit fairly frequently if you anticipate significant tax bill for the year.

Cumulative Cash Levels: The closing cash balance is the amount you started out with plus or minus the amount of cash surplus or deficit at month end. This cumulative total becomes your opening cash balance for the next month.

SUMMARY

A cash flow analysis assists in financial planning, inventory purchases and formulating credit and collections policies. It also serves as an early indicator when expenses are getting out of line. It is one of the most important tools an owner/manager has to control his or her business.

It is important to stress once again that a cash flow is an ongoing business tool that needs to be revised as the situation changes. A computer spreadsheet is very **useful** for this purpose. After each month has been completed, put the actual cash flow figures next to the panned figures and compare them. If the planned figures vary considerably with the actual, it may be necessary to revise the figures for succeeding months. In extreme situations it may be necessary to rethink the particular aspects of the business operation.

Source: The Government of British Columbia

CASH FLOW FORECAST FOR FIRST 12 MONTHS OF OPERATION

	1	2	3	4	5	6	7	8	9	10	11	12	TOT
Estimated Sales (monthly)													
Cash Receipts													
Cash from Sales *													
Other (specify)													
Cash Equity Contribution													
Government Loans													
Bank Loan													
Total:													
Cash Disbursements													
Purchase of Equipment													
Rental Expenses													
Labour Expenses													
Personal Drawings													
Materials													
Licenses and Insurance													
Advertising													
Selling Expenses													
Office Expenses													
Other (specify)													
Loan Payments													
Income taxes													
Total:													
NET CASH: Total Cash Receipts minus Total Cash Disbursements = $													
Monthly Net Cash Surplus													
Monthly Net Cash Deficit													
Cumulative (to date)													
* If your business grants credit, only include cash that will actually be collected.													

The Financial Plan – Part 1

The financial plan is perhaps the most important component of your business plan. Not only is it essential in obtaining financing but poor financial planning is one of the biggest factors in business failure.

The financial plan will look at costs associated with operating your business, the collection of potential sales and the cost of sales in order to put you in a better position to reasonably forecast your financial projections.

The first step is to determine your start-up financial requirements.

A. Estimated One-Time Financial Requirements.

Indicate your estimate of the start-up financial requirements of your business if it is a new venture.

	Item	**Estimated Cash Required**
1	Business Registration	$
2	Licenses and/or permits	
3	Starting inventory	
4	Start-up loan and interest payments	
5	Professional start-up fees (lawyers, accountant, etc)	
6	Furniture, fixtures and office equipment	
7	Machinery and equipment	
8	Installation of equipment	
9	Tools and supplies	
10	Signage	
11	Security	
12	Down payment on purchase of or deposit on the lease for business premises	
13	Building improvements	
14	Utility hook-up and installation fees	
15	Pre-opening advertising and promotion	
16	Cash reserve	
17	Other	
18	Other	
	Total Estimated One-Time Requirements	$

B. Estimated Start-up Operating Expenses

	Item	Estimate of Monthly Expenses	Number of Months Before Breakeven	Total Cash Required
1	Rent/Lease	**$**		**$**
2	Utilities			
3	Line of Credit			
4	Insurance			
5	Ongoing professional fees (accountant, lawyer)			
6	Depreciation			
7	Business taxes			
8	Operating loan if needed			
9	Interest on operating loan			
10	Inventory			
11	Owner's salaries			
12	Employees payroll, benefits and remittance			
13	Phone (including long distance)			
14	Postage and supplies			
15	Promotion and advertising			
16	Credit sales to customers			
17	Cash discounts to customers (2%)			
18	Maintenance and repairs			
19	Travel and vehicle			
20	Other			
21	Other			
Total Cash Requirements for Operating Expenses				**$**
Plus Total One-Time Cash Requirements				**$**
Total Cash Required for Start-Up				**$**

Estimate your source of funds by providing an overview of the current finances contributed to the start-up of the business to date.

C. Sources of Funds

	Source	Amount	Debt or Equity	Repayment Schedule
1	Self	$	$	$
2	Friends, neighbours, relatives			
3	Other private investors			
4	Banks, savings and loans, credit unions and other financial institutions			
5	Mortgage and insurance companies			
6	Credit from suppliers			
7	Government grants and loans			
8	Other sources:			
Total:		$	$	$

The Financial Plan – Part 2

Once you have determined your start-up financial requirements, you will need to develop your short-term financial projections.

Estimate your total expected revenue and expenses for at least the first year of business. This projection will show your predicated sales volume, cost of production or purchase of products, fixed and variable monthly operating expenses and your expected net operating profit or loss.

D. Pro Forma Income Statement

Business Name

Pro Forma Income Statement

For the year ending (date)

Net sales		
Less: cost of goods sold		
Beginning inventory		
Plus: net purchases		
Goods available for sale		

Less: ending inventory		
Cost of goods sold		
Gross margin		
Less Operating expenses:		
Employee wages		
Supplies		
Advertising and promotion		
Delivery, freight		
Travel and entertainment		
Professional fees		
Rent		
Phone and utilities		
Property taxes		
Business taxes		
Repairs and maintenance		
Depreciation		
Interest		
Insurance		
Other		
Total Expenses		
Net Profit (Loss) before Income Tax		

E. Pro Forma Balance Sheet

Business Name

Opening Balance Sheet

As of (date)

ASSETS		
Current Assets		
Cash		
Accounts Receivable		
Inventory		

Other		
Total Current Assets		
Fixed Assets		
Building		
Furniture and fixtures		
Equipment		
Trucks and vehicles		
Other		
Total Fixed Assets		
Total Assets		
Liabilities		
Current Liabilities (due within 12 months)		
Accounts payable		
Bank loans/other loans		
Taxes owed		
Total Current Liabilities		
Long-term Liabilities		
Mortgages payable		
Loans from partners/shareholders		
Other		
Total Fixed Liabilities		
Total Liabilities		
Net Worth (Capital)		
Total net Worth (Assets-Liabilities)		
Total Liabilities plus Net Worth		

Statement of Net Worth

______________________**(DATE)**

Assets

Cash in bank	$
Accounts receivables	
Merchandise	
Antiques, collections, etc.	
Stocks	
Bonds	
Loans receivable	
RRSP	
Pension	
Total Liquid Assets	$
Mortgage receivable	**$**
House	
Cottage	
Other real estate	
Cars	
Other vehicles	
Total of all Assets	**$**

Liabilities

Bank loans (car, RRSP)	**$**
Other loans	
Other loans	
Credit cards	
Loans, notes payable	
Mortgages	
Other mortgages	
Other	
Total Liabilities	**$**

Assets – Liabilities = Net Worth	