

Cash Flow Management Made Easy

by Robert A. Normand

SUMMARY: Cash Flow forecasting is as important as monitoring profitability. Four to eight week forecasts should project the cash position at the end of each week and assure that it is adequate to meet the cash requirements of the following period. If there is too little cash, then cash paid out must be reduced temporarily, possibly by delaying payments on certain line items to particular vendors or cash must be injected into the business from a reserve, line of credit or other sources.

Small business owners soon learn that Cash Flow and Profit are not one and the same thing. The two may be related but are not always in concert. There can be high profits reported during a period of extremely tight cash flow and low profits reported during a cash rich period.

Profitability is based on *invoicing* and the relationship of costs, either expended or accrued, to those sales. The actual payment of expenses or receipt of invoice payments can, and often do, occur in periods different than when the sales occurred, so that cash flow can be widely different from reported profit in any period.

Cash Flow is based on changes in cash balance and can be affected by changes in assets that don't affect profitability. Allowing inventories to build or accounts receivable to go uncollected and grow can have a tremendous cash draining effect on the business. In effect you are converting cash to an *investment* in these other assets. Investments take cash out of the business.

During a period of strong growth even a very profitable business can (and usually will) experience cash flow problems. Therefore, corporate growth or sales success should not be viewed as a reason to stop performing a cash flow forecast. On the contrary, it is more important, even critical, that management has access to timely cash management information during growth periods.

Just as many businesses have succumbed to poor cash management as have been adversely affected by bad profitability. It is imperative, therefore, that cash be monitored and managed efficiently, separate and apart from budgeting and auditing of profit performance.

There are two types of cash flow forecasting that can be done: short term and long term. We focus in this article on short term forecasting only.

What a Cash Flow Forecast Is and Does

A cash flow projection is a forecast of anticipated cash expenditures and receipts over a time span. Typically for short term forecasting the time period is expressed in weeks and covers a projection of 4 to 8 weeks out. As a minimum, the cash flow forecast should take into consideration the following possibilities:

CASH RECEIVED (each week):

Cash Balance Day1, Week 1

Cash Sales

Accounts Receivable Payments

Draw from Line of Credit

Loan Proceeds or Stockholder Funding

Miscellaneous Income

CASH EXPENDITURES – RECURRING EXPENDITURES

Payroll

Payroll Taxes & Fees

Rent/Mortgage
Utilities (Gas & Electric, Water/Sewer/Trash)
Telephone (Office, Cell, Pagers/Answering Services)
Computer Services (Internet, Maintenance, Equipment Lease)
Other Equipment Leases or Loan Payments
Vehicle Lease and Loan Payments
Insurance (Health, Business, Life, Property)
Loan Paybacks
CASH EXPENDITURES – ACCOUNTS PAYABLE
Vendor Payments for Merchandise (by Invoice)
Vendor Payments for Services (by Invoice)
All Other Non-Recurring Payments

You can devise a spreadsheet that accounts for all these items or purchase a pre-designed system that automates the forecasting process and tracks payments, including the ability to adjust receipt and payment dates quickly and easily. One such system is available at the reference given at the Bio at the end of this article.

The goal of cash flow forecasting is to determine deficiencies or excesses in cash position that may occur in the business during the periods for which the projection is prepared. In the event projected cash balance goes negative or below a safety factor, financial plans must be altered, either to provide more cash through aggressive collections, loans, draws on lines of credit, increased (cash) sales, and/or delaying payments as necessary, until a proper cash balance is reached.

If excessive cash is projected, it may indicate idle money that could be put to other possible uses such as prepaying expenses or for investment into short-term money market instruments.

The objective is to develop a plan that, if followed, will provide a well-managed flow of cash and its efficient, optimum use.

© Institute for *Smart Business Management*, Inc. All Rights Reserved

Author: Robert A. Normand (www.bobnormand.com) is Executive Director of the Institute for *Smart Business Management* (www.isbminc.com) and author of "*Entrepreneur*, The Six Step Recovery Program for Small Business" (www.entrepreneur.com).

Mr. Normand has served as principal management consultant for more than 100 businesses ranging from \$500,000 to \$50,000,000 in annual sales and has owned and operated several small businesses of his own in diverse industries. Mr. Normand's small business philosophy is premised on the belief that small business management skills can be developed by busy entrepreneurs using readily available information, tools and procedures not found in business schools or formal degree programs. He can be reached by telephone at 941-330-0889 or by e-mail to bob@bobnormand.com.

For more information on Strategic Planning problems facing owners/entrepreneurs and their solutions, see our *QuickStart Operating Procedures*®, "Planning Solutions" section at www.isbminc.com.