Cash Flow is King! Plan Accordingly

In the last blog post we talked about creating an operating budget. This is a blueprint of your operations to help you chart the growth of your company. Where an operating budget is a planning document that is designed to give you a way to plan for the company's growth, a cash flow forecast helps you keep track of immediate costs to keep the company running.

In many ways, a cash flow forecast is more important than an operational budget. Many businesses have failed because they are so focused on the their future growth that they fail to worry about managing their daily operations and run short of cash to deal with critical expenses such as payroll and rent. By creating a cash flow forecast you can map income to outflow in a way that you can ensure you keep the lights on so you can reach your long-term goals. You need to plan your cash allocations for the week, the month, and the year.

INFLOWS

1. Determine what your receivables look like. If your payment terms are typically net 30 days, then you can expect most customers or clients to pay within 45 days. Use this as a basis for your income forecast. For example, assume that your January invoices will be paid in March. Be sure to carry over any outstanding invoices from the previous fiscal year. Also be sure to make allowances for clients you know to be regularly delinquent with their payments.

2. Identify any additional cash receipts or income. Do you have additional sources of income from rent, bank loans, equity transactions, refunds, customer deposits, or anything else that generates cash?

OUTFLOWS

1. Look at expenses and cash disbursements. If you have already created an operating budget, then you should have a solid idea of what your fixed cash expenses are. These are going to be immovable costs such as payroll, electricity, rent, and the like. Also identify any additional expenses you are predicting, such as travel costs, entertainment, bonuses, or any planned expenses that don't fit in the regular monthly P&L. And be sure to include costs for fixed asset purchases, such as new equipment or loan payments.

2. Review the accounts payable balance from the previous year (or months) and look for items that still need to be paid. Be sure to include those in your cash planning – when will you pay these debts? However, be sure not to include amortization or depreciation in your planning; these don't impact your cash on hand.

3. Consider any capital outflows, such as loans coming due, equipment purchases or owners draws.

The difference between your inflows less your outflows will determine how much cash will be added or subtracted from your cash position each month. Now you have a clear picture of your cash flow, including income and expenses. Use accounting software packages or an Excel spreadsheet to make this an efficient process. Be sure to share your cash flow budget with key managers to make sure you haven’t overlooked an expense, and so they can help you reach your monthly goals. And share it with your Controller/CFO so they can help you stay on track.

Remember that your cash flow forecast is a living document and it will change from month to month. Be sure to revisit and revise it often as you add new customers and new expenses. The best strategy is to review your cash flow budget at the start of each month, identifying accounts receivable and accounts payable. Add to your invoices estimates of payment collections you can expect. And keep track of your payments during the month to make sure you stay within your projections and your payments don’t exceed your income.

Cash is the life’s blood of any company, so managing cash flow is critical to your day-to-day operations. If you carefully track your income against your outflow, and correct your assumptions as necessary along the way, you can stay cash positive on a monthly basis, which will help you manage more effectively to reach your long-term operational goals.