

Although profits from a business venture are a measure of success, the flow of cash in and out of a business can be said to be its lifeblood. Cash flow planning is critical to the survival and growth of a business. Unless cash is available at the time it is required, the business may have to close its doors, even though profits are being earned.

Overview

A sensible forecast will help stabilise the cash flow pattern and enable you to meet seasonal commitments and plan for expenditure on new equipment or expansion. It will also forecast when additional funds may be required; both short and long term.

The main method of preparing a cash flow forecast is by estimating cash receipts and payments for a projected period. This period of projection is usually for twelve months on a monthly basis.

The following is an example of how to budget:

Forecast sales (income)

The budgeting process will ascertain potential future turnover on a monthly basis for the period ahead. A new business should develop a monthly budget based on market research and development already undertaken. It is unwise to be over-optimistic. Only proceed on the basis of figures which you are confident can be achieved.

Projected cash receipts

When budgeting for anticipated sales, depending on the business you are in, you may need to allow for sales made on credit, usually by way of an account which will have an agreed payment term of 14 days, 30 days etc.

Estimated payments (expenses)

Payments are usually classified as either:

- Fixed expenses – expenses which do not vary with the volume of the business. An example of these expenses is rent, salaries and wages, insurance and a portion of telephone.
- Variable expenses – those expenses which may increase with the volume of business being conducted each month and which may have some impact on future months such as the amount stock held, depending on different times of the year (ie Christmas, Mother's days etc.)
- Periodical payments – amounts that must be covered are lease charges, loan repayments, taxation and interest on bank loans.

Net Cash Movement

Having compiled the estimated cash receipts and payments, you can then ascertain the surplus or deficit in cash indicated by the monthly figures. From these figures, you can include the balance at the beginning of the period, and then by addition (for a surplus) and subtraction (for a deficit) this will then indicate your monthly cash flow requirements.

	July	Aug.	Sept.	Oct.
A Cash Sales	\$1 000	\$1 500	\$700	\$1 200
B Credit Sales (due in 30 days)	\$4 000	\$5 000	\$5 300	\$5 800
C Total Sales (A + B)	\$5 000	\$6 500	\$6 000	\$7 000
D Total Cash Receipts	<u>\$1 000</u>	<u>\$5 500</u>	<u>\$5 700</u>	<u>\$6 500</u>
E Less: Expenses	\$3 500	\$4 000	\$4 400	\$5 300
Profit (C – E)	\$1 500	\$2 500	\$1 600	\$1 700
Monthly Cash Balance (D – E)	<u>-\$2 500</u>	<u>\$1 500</u>	<u>\$1 300</u>	<u>\$1 200</u>
Running Cash Balance	-\$2 500	-\$1 000	\$300	\$1 500

Bank Facility

From the above you will then be able to determine whether you will need a bank overdraft or inject further capital into the business to cover the cash flow requirements.

Summary

The cash flow budget should cover a minimum period of 12 months and it may be prudent to further expand this for a further 6 – 12 months. Once a budget has been finalised it is a good management practice to monitor the budgeted figures against the monthly actuals, at the end of each month. A simple way to achieve this is by adding another column alongside each months' budget amounts. Obviously, any large discrepancy should be immediately investigated and if required adjustments made for the ensuing months.

Need More Help?

Your accountant is best placed to help you prepare a cash flow budget. Your Territory Business Centre also has workshops and aids to assist you in preparing a cash flow budget, visit the TBC website at www.tbc.nt.gov.au.

For more information refer to other Fast Facts in this series or contact the Territory Business Centre on the numbers below or visit the TBC website.

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