

Preparation of a cash flow forecast

Cash flow forecast

Cash flow relates to the amount of money received and spent in a given period. Cash flow problems occur when the amount spent is greater than the amount received. You may have cash flow problems from time to time-especially just before pay day-when you are short of cash to buy or do what you want. Unless you want to get into debt you need to reduce your spending until you get more money.

Businesses can also have cash flow problems. This may be because some people who owe them money have not paid their bills when they should. The business then does not have enough money in the bank to pay the bills it has received from its suppliers.

Businesses use cash flow forecast to predict how much money they should have in the bank at any particular time, usually at the end of a month. This means listing and adding up all their expected cash inflows.

Cash inflow

Cash inflows are money received by the business for variety of reasons such as the capital, which means the money that the owner puts into the business at the start and sales.

Cash outflow

Cash outflow is the money that goes out such as purchases for example manufacturing businesses will buy raw materials, wages, rent etc

In flows is the money the business expects to receive and pay into its bank account. It then needs to add up its cash out flows. This is the difference between these two figures is the cash balance. Every business will always aim for a positive cash balance, which occurs when inflows are greater than outflows.

Poor cash flow

The problem a poor cash flow can create for a business is they might run out of money and not pay their bills on time

Wooden Wonders credit control

Wooden wonders can minimize these cash flow problems through a better control by making sure they are paid on time and make payments as late as possible.

Situation 1

	January	February	March	April	May	June
Inflow						
Sales	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Total inflow	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Cost of sales	£1,750.00	£2,000.00	£2,250.00	£2,500.00	£2,750.00	£3,000.00
Rent	£2,000.00	£2,000.00	£2,000.00	£2,000.00	£2,000.00	£2,000.00
Insurance	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Electricity	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Total outflows	£3,850.00	£4,100.00	£4,350.00	£4,600.00	£4,850.00	£5,100.00
Net cash flow	£350.00	£100.00	£150.00	£400.00	£650.00	£900.00
Opening balance	£5,000.00	£4,650.00	£4,550.00	£4,700.00	£5,100.00	£5,750.00
closing balance	£4,650.00	£4,550.00	£4,700.00	£5,100.00	£5,750.00	£6,650.00

In the first 3 months January, February and March Wooden Wonders had a poor cash flow. As the sales increased in the following months Wooden Wonders have a positive cash flow and have no more problems with its cash flow so that if the business continues in this way it will run effectively.

Situation 2

	January	February	March	April	May	June
Inflow						
Sales	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Total inflow	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Cost of sales		£1,750.00	£2,000.00	£2,250.00	£2,500.00	£2,750.00
Rent	£2,000.00	£2,000.00	£2,000.00	£2,000.00	£2,000.00	£2,000.00
Insurance	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Electricity	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Total outflows	£2,100.00	£3,850.00	£4,100.00	£4,350.00	£4,600.00	£4,850.00
Net cash flow	£1,400.00	£150.00	£400.00	£650.00	£900.00	£1,150.00
Opening balance	£5,000.00	£6,400.00	£6,550.00	£6,950.00	£7,600.00	£8,500.00
closing balance	£6,400.00	£6,550.00	£6,950.00	£7,600.00	£8,500.00	£9,650.00

Wooden Wonders has given raw materials suppliers one month credit, so this made the business run better and make a positive cash flow, as you can see above the total inflows is more than the total outflows, which definitely means that the net cash flow is the profit which remains to the business, from the starting cost of £5,000 in January to £9,650 June which is £4,650 profit in 6 months, if the business continues this way it will run efficiently.

Situation 3

	January	February	March	April	May	June
Inflow						
Sales	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Total inflow	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£5,500.00	£6,000.00
Cost of sales	0	£1,750.00	£2,000.00	£2,250.00	£2,500.00	£2,750.00
Rent	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00
Insurance	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Wages	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00
Electricity	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Total outflows	£2,100	£4,350.00	£4,600.00	£4,850.00	£5,100.00	£5,350.00
Net cash flow	£900.00	-£350.00	-£100.00	£150.00	£400.00	£650.00
Opening balance	£5,000.00	£5,900.00	£5,550.00	£5,450.00	£5,600.00	£6,000.00
closing balance	£5,900.00	£5,550.00	£5,450.00	£5,600.00	£6,000.00	£6,650.00

Although the rent is reduced to £1,500 Wooden Wonders have to pay £1,000 wages. In January Wooden Wonders did not have cost of sales, so this was a good start for the business but in February and March the net cash flow was negative, but this did not harm the cash flow because they had profit to back them up from January, in the following months the cash flow was positive, this means if the business continues like that it will run effectively.

Situation 4

	January	February	March	April	May	June
Inflow						
Sales	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£2,500.00	£6,000.00
Total inflow	£3,500.00	£4,000.00	£4,500.00	£5,000.00	£2,500.00	£6,000.00
Wages	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00
Cost of sales	£0.00	£1,750.00	£2,000.00	£2,250.00	£2,500.00	£2,750.00
Rent	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00
Insurance	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Electricity	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Total outflows	£2,600.00	£4,350.00	£4,600.00	£4,850.00	£5,100.00	£5,350.00
Net cashflow	£900.00	-£350.00	-£100.00	£150.00	£2,600.00	£650.00
Opening balance	£5,000.00	£5,900.00	£5,550.00	£5,450.00	£5,600.00	£3,000.00
closing balance	£5,900.00	£5,550.00	£5,450.00	£5,600.00	£3,000.00	£3,650.00

The cash flow for this situation is similar to the one I mentioned above except in May a customer goes busted and didn't pay his money, so this affected the cash flow, by leaving

the net cash flow negative. So if the business stays like that, it will earn back its losses in the next few months and have a positive cash flow.

	<u>Situation 5</u>					
	January	February	March	April	May	June
Inflow						
Sales	£0.00	£0.00	£3,500.00	£4,000.00	£4,500.00	£8,000.00
Total inflow	£0.00	£0.00	£3,500.00	£4,000.00	£4,500.00	£8,000.00
Wages	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00	£1,000.00
Cost of sales	£0.00	£1,750.00	£2,000.00	£2,250.00	£2,500.00	£2,750.00
Rent	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00	£1,500.00
Insurance	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Electricity	£50.00	£50.00	£50.00	£50.00	£50.00	£50.00
Total outflows	£2,600.00	£4,350.00	£4,600.00	£4,850.00	£5,100.00	£5,350.00
Net cashflow	£2,600.00 ⁻	£4,350.00 ⁻	£1,100.00 ⁻	-£850.00	-£600.00	£2,650.00
Opening balance	£5,000.00	£2,400.00	£1,950.00 ⁻	£3,050.00 ⁻	£3,900.00 ⁻	£4,500.00 ⁻
closing balance	£2,400.00	£1,950.00 ⁻	£3,050.00 ⁻	£3,900.00 ⁻	£4,500.00 ⁻	£1,850.00 ⁻

Wooden Wonders customers demand that they be given two months credit this has harmed the cash flow and made a negative cash flow for the company. This is because the money that is going out (out flows) is more than the sales, which kept the net cash flow negative for the first five months. In June the net cash flow changed positively, because the customer that went busted paid the £3000 back, but this still didn't make a positive cash flow. This is still a loss for Wooden Wonders because the closing balance for June is less than the opening balance for January. If the business stays like that, it might take a long time to earn back the money the business started with, which is the opening balance and in the next few months the cash flow might get better.