

Topic 1.3.3 Cash flow forecasting

Key Vocabulary

Cash – the money a business holds in notes and coins and in its bank accounts

Cashflow – the movement of money in and out of a bank account

Insolvency – when a business lacks the cash to pay its debts

Overdraft – the amount of an agreed overdraft facility that a business uses; when a business has a negative bank balance

Overdraft facility – the maximum amount that a business is allowed to go into negative balance on its bank account

Cash inflows – money entering the bank account, e.g. from sales

Cash outflows – money leaving the bank account, e.g. bills for supplies

Net cash flow – inflows minus outflows

Opening balance – the amount of money at the start of the month

Closing balance – the amount of money at the end of the month; Opening balance ADD net cash flow

Core Knowledge

A business will **predict** the amount of money that will enter and leave the business each month.

This allows the business to identify any periods of shortfall, to plan how to deal with this.

Businesses need cash to pay suppliers, employees and all the overheads.

Difficulty can arise if businesses allow customers to pay on **credit**.

Cash needs to be managed by arranging an overdraft, keeping costs down, keeping inflows up

Improve cash flow by cutting stock levels, increase credit from suppliers, reduce credit to customers

	Aug	Sept
Cash inflows	0	85
Cash outflows	185	75
(A) Net cash flow	-185	10
(C) Opening Balance	250	65
(B) Closing balance	65	75

(A) Net cash flow = inflows - outflows

(C) Closing Balance = Opening + Net Cash flow

(B) Opening Balance = last month's closing balance

Wider Business World

Retailers – they often have seasonal or unsteady cash flow as they need to buy stock before they can sell it

Hotels / restaurants - may have seasonal business, so it will be important to build up a balance to support them through periods of low sales



Synoptic Links

Costs & Revenue – know which items are revenue (inflows) and which are costs (outflows)

Sources of finance – if outflows are greater than inflows, short term finance is needed

Don't be a "man on the street"

- Do not confuse cash & profit – they are very different things
- A cash flow forecast is a prediction not what has happened
- An overdraft does not mean the business will fail – it simply means that in that month outflows exceeded more than inflows. Debt is not always a bad thing!
- Lots of cash in the bank is not always a good thing – this could be invested to improve the business