

How to Understand Cash Flow Statements

Manage Your Benjamins

What is a Cash Flow Statement?

Cash flow is the combination of **the amount** of money coming in and going out of your business and, critically important to your operations, **the timing** of cash movements.

Therefore, a Cash Flow Statement maps sales to customers and when you pay bills, especially payroll. Diligently tracking the money coming in and out of your business is very important because even profitable businesses can fail if they don't have the right amount of cash available at the right time.

Here are some key terms for you to review as you explore Cash Flow Statements.

- **Amortization:** an accounting method used to spread the cost of an intangible asset, such as reputation or goodwill, over the course of the asset's life. It functions in the same way as depreciation for tangible assets.
- **Asset:** something owned by a company that holds value; assets can be physical, like equipment and inventory, or nonphysical, like trademarks and patents or goodwill.
- **Balance Sheet:** a statement that shows your company's assets, liabilities and owners' equity to indicate financial health at a specific point in time. The goal of a Balance Sheet is to make sure that your company's assets are equal to the combination of your liabilities and owners' equity, i.e., $\text{Assets} = \text{Liabilities} + \text{Equity}$ (Net Worth). As such, it shows your collection of total assets plus how they were paid for.¹
- **Cash Flow Statement:** a document showing the timing of all cash going in and out of the business over a particular period of time.

- > **Current Assets:** the sum of cash and cash equivalents, accounts receivable, inventory, marketable securities, prepaid expenses and other assets that could be converted to cash in less than one year.²
- > **Current Liabilities:** the sum of all money owed by a company and due within one year.³
- > **Depreciation:** a calculation to show how your tangible assets lose value over time. While there are several ways to account for depreciation, the most basic is for an asset's salvage value subtracted from its cost to determine the amount to be depreciated.
- > **Income Statement:** a statement that shows how your business has performed over a given period—the amount of profit or loss generated.⁴
- > **Liabilities:** obligations that the company owes, either to vendors, suppliers, and lending institutions.
- > **Cash Position:** the amount of cash you have available for use.

How to Use a Cash Flow Statement

To use a Cash Flow Statement, you'll typically take the following steps:

1. Enter the **starting balance**, which is the **cash on hand** from your Balance Sheet.
2. Enter the amount and time when **cash came into** your business.
3. Enter the amount and time when **cash went out** of your business.
4. Subtract the amount of cash **going out** from the **amount coming in**. This number will give you your **cash position**. Looking at this over time gives you your **cash flow**.

Before we explore a Cash Flow Statement, let's first look at a cash flow planner.

CASH FLOW PLANNER

Below, you'll find a cash flow planning tool (planner). This planner will help you see, in detail, the cash inflows and outflows before you explore a detailed example of a Cash Flow Statement later in this section.

The planner below has been created for Jayne's Locksmith Company (JLC), a small business that installs locks in commercial buildings.

When using this cash flow planner for your business, change the category labels in the left column as necessary to fit your accounting system.

As you review this planner, ask yourself line by line when you should expect cash to come and go.

- Predict when you'll actually collect from customers.
- On the expense side, predict when you'll actually have to write the checks to pay those bills. For example, **rent** and **utility** bills are usually paid in the month they are incurred. **Insurance** and some types of **taxes** may actually be payable quarterly or semiannually, even though you recognize them as monthly expenses.

EXAMPLE: CASH FLOW PLANNER (12-MONTH) FOR JAYNE'S LOCKSMITH COMPANY (JLC)

Note: All numbers within closed brackets () are negative numbers.

	Q1	Q2	Q3	Q4	Total	Notes	Total Item
Cash on Hand (beginning of month)	\$179,248	\$251,753	\$281,008	\$288,113	\$335,376	This figure comes from the Balance Sheet.	
CASH RECEIPTS							
Sales	\$146,000	\$128,000	\$223,000	\$250,000	\$747,000	Total sales for the year is \$747K. This figure comes from the Income Statement.	
Collections from A/R accounts/CR accounts	\$22,000	(\$7,000)	(\$8,000)	\$5,000	\$12,000	In Q1 JLC collected \$22K of the \$26K of A/R due from last year. Q2 and Q3 A/R increased. In Q4, JLC collected as much as possible. TOTAL: The change in account receivables is \$12K.	

	Q1	Q2	Q3	Q4	Total	Notes	Total Item
CASH RECEIPTS							
Loan/other cash injection			\$150,000		\$150,000	Q3 loan of \$150K on a \$175K machine. \$25K difference between machine cost and JLC loan amount is down payment.	
Total Cash Receipts	\$168,000	\$121,000	\$365,000	\$255,000	\$909,000		
Total Cash Available (before cash out)	\$347,248	\$372,753	\$646,008	\$543,113	\$1,244,376	Cash on hand + total cash receipts	
CASH PAID OUT							
Purchase (merchandise) cash	\$2,300	\$3,000	\$21,500	\$12,90	\$39,700	Q1: \$2,300K worth of purchases in cash Q2: \$3K, etc	
Purchase (merchandise) A/P (accounts payable)			\$42,300	\$27,600	\$69,900	Purchases made on account	
A/P payments (- increases)	\$2,000	\$3,000	(\$16,000)	\$10,000	(\$1,000)	In Q1, paid \$2K of last period's A/P	
Gross wages (exact withdrawal)	\$45,000	\$42,000	\$61,000	\$77,000	\$225,00	Paid salaries/ wages. Wages increased with the addition of machinist.	
Payroll expenses (taxes, etc.)	\$6,750	\$6,300	\$9,150	\$11,550	\$33,750	Payroll expense is 15% of gross wages.	
Outside services					0		
Supplies (office & oper.)	\$2,500	\$2,000	\$10,000	\$5,500	\$20,000	Q3: larger supply expense in preparation for manufacturing	
Repairs & maintenance					0		

	Q1	Q2	Q3	Q4	Total	Notes	Total Item
CASH PAID OUT							
Advertising	\$1,000	\$500	\$1,500	\$2,000	\$5,000	Variation in expenditure in Q3 and Q4 due to new services. Also, JLC typically spends more on advertising at the end of the year.	
Car, delivery & travel	\$2,600	\$2,600	\$2,600	\$2,600	\$10,400	Car allowance figure comes from income statement.	
Accounting & legal					0		
Rent	\$12,000	\$12,000	\$12,000	\$12,000	\$48,000	Rent comes from income statement.	
Telephone	\$845	\$845	\$845	\$845	\$3,380	Telephone costs come from income statement.	
Utilities	\$4,500	\$3,500	\$6,000	\$7,000	\$21,000	Utility expense increased at end of year based on season and running of the machine.	
Insurance	\$4,000	\$4,000	\$8,000	\$8,000	\$24,000	Increase in insurance due to machine operation	
Taxes (real estate, etc.)			\$2,400		\$2,400	Personal property tax on machine due	
Interest			\$4,500	\$4,500	\$9,000		
Accrued expense/ payable (decrease-increase)			(\$2,400)	(\$3,500)	(\$5,900)	Money JLC has not paid. On balance sheet \$3,500 owed for payroll taxes. \$2,400 owed for personal prop taxes. Both payments are owed at the end of the period and paid next year.	
Income taxes	\$12,000	\$12,000	\$12,000	\$22,242	\$58,242		
Other (specify)					0		
Miscellaneous					0		

	Q1	Q2	Q3	Q4	Total	Notes	Total Item
CASH PAID OUT							
Subtotal	\$95,495	\$91,745	\$175,395	\$200,237	\$562,872		0
Loan principal payment			\$7,500	\$7,500	\$15,000	Q3 and Q4 payment on loan for machine bought on July 1 Loan principal payment takes cash out of the business and, therefore, is an important factor to include in the cash plan.	
Capital purchase (specify)			\$175,000		\$175,000	Q3 and Q4 payment on machine bought on July 1 Capital purchases take cash out of the business and, therefore, are an important factor to include in the cash plan.	
Other startup costs					0		
Reserve and/or escrow					0		
Owner's withdrawal					0	Owner's draw takes cash out of the business and, therefore, is an important factor to include in the cash plan.	
Total Cash Paid Out	\$95,495	\$91,745	\$357,895	\$207,737	\$752,872		0
Cash Position (end of month)	\$251,753	\$281,008	\$288,113	\$335,376		Monitor the cash position. If it gets too low or negative, JLC will need to pump in more cash to keep the operation going.	\$179,248

	Q1	Q2	Q3	Q4	Total	Notes	Total Item
ESSENTIAL OPERATING DATA (non-cash flow information)							
Note: This section is not actually part of the cash model, but it allows you to track items that have a heavy impact on cash.							
Sales volume (dollars)							
Accounts receivable							
Bad debt (end of month)							
Inventory on hand (end of month)							
Accounts payable (end of month)							
Depreciation							

Note: The example above has been created using modified [SCORE Excel templates](#).

SAMPLE CASH FLOW STATEMENT

Cash flow projection is the best way to teach you how to meet your working capital needs. Your historic Cash Flow Statements can guide you in projecting your future cash flow to help you plan for the future.

EXAMPLE: JAYNE’S LOCKSMITH COMPANY (JLC)

This example Cash Flow Statement shows how JLC manages their cash by selling locks to customers and continuing commercial and residential installations. Note: Cash Flow Statements for accounting purposes reflect less information than a cash flow planning worksheet. For more details, please refer to the cash flow planner above, and use the template to create your own planner.

Note: All numbers within closed brackets () are negative numbers.

	Y1	Notes
Cash flows from operating activities		
Net income	\$35,520	The net income figure comes from the Income Statement.
Adjustments to reconcile net income to net cash used in operating activities		
Depreciation and amortization	0	This figure depicts the noncash expense. Depreciation is listed in the Income Statement.
Changes in operating assets and liabilities		
Accounts receivable	0	This data comes from the Balance Sheet. Note: Increasing assets reduce cash, and increasing liabilities increase cash. Here, JLC is seeing an estimated decrease of \$12,000 (\$26K to \$14K).
Inventories	0	From the Balance Sheet. Note: Increasing assets reduce cash, and increasing liabilities increase cash. JLC is seeing an estimated increase of \$10,000 (from \$12K to \$22K).
Other current assets	0	
Accounts payable	0	These numbers come from the Balance Sheet. Y3 has \$1K increase in accounts payable.
Other current liabilities	0	These numbers come from the Balance Sheet.
Total adjustments	0	
Net cash from operating activities	\$35,520	

	Y1	Notes
Cash flows from investing activities		
Purchase of property and equipment	0	Fixed assets on the Balance Sheet JLC will buy the machine. The projected cost is \$175, out of which \$25K is down payment.
Investment purchase	0	
Net cash used in investing activities	0	
Cash flows from financing activities		
Proceeds from notes payable	0	Loan for equipment (less down payment) JLC's down payment = difference between \$175K and \$150K. Depreciation for this shows up on the Income Statement.
Change in long-term debt		Paid down note on machine by \$15K
Change in owner-invested capital	0	
Net cash provided by financing activities	0	
Net increase (decrease) in cash and cash equivalents	\$35,520	
Cash and cash equivalents, beginning	\$50,000	This is the same as the figure at the end of the previous year. It depicts the beginning cash for next year.
Cash and cash equivalents, ending	\$85,520	

Note: The example above has been created using modified SCORE Excel templates.

How to Use a Cash Flow Statement

Cash Flow Statements help you manage the timing and amount of money coming in and out of your business over a specific period of time.

Use the cash flow planner resource provided for this tool to practice creating a cash flow planner for your business.



Disclaimer: *The business appearing in this work is fictitious. Any resemblance to an actual business is purely coincidental.*

¹ *Start with a Balance Sheet*, U.S. Small Business Administration, <https://www.sba.gov/business-guide/manage-your-business/manage-your-finances#section-header-0> (accessed April 11, 2019)

² *Glossary of Business Financial Terms*, U.S. Small Business Administration (June 20, 2018), <https://www.sba.gov/document/support-glossary-business-financial-terms> (accessed April 11, 2019).

³ *Ibid.*

⁴ *How to Prepare a Loan Package*, https://www.sba.gov/sites/default/files/How_To_Prepare_a_Loan_Package_Transcript.pdf (accessed April 11, 2019).