# Cashflow Forecasts

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# Overview

For start-ups and established businesses alike, the preparation and regular review of a cashflow forecast is essential if you want to maximise profits.

Not sure where to start? No problem, we are here to help, and we are confident that this guide will provide you with all the tools you need to get up and running.

Prefer to leave it to the experts? Great! Get in touch for a free 15-minute consultation with one of our in-house management accountants today.

## What you need to know

### What is a cashflow forecast?

A cashflow forecast is a report which helps you to estimate the amount of money which will move in and out of your business's bank accounts over a given period, typically a year.

Creating a cashflow forecast will help you identify and plan spending patterns in advance. This will allow your business to take advantage of times when cash is abundant, but also avoid running out of cash when large bills need paying.

As time passes, you can go back and compare your forecast with your actual results and see how your business performed against expectations.

### Why is it important to prepare a cashflow forecast?

Even with strong client interaction and billing, receiving cash from your customers can often be a slow process. It's not uncommon for a business to have strong sales and struggle with cashflow as a result of collection delays.

It doesn't take long for slow recovery of client fees to seriously impact a business's ability to make payments to demanding suppliers and landlords. Understanding both the sources and certainty of cash movements will give you the foresight to ensure your business always has enough cash in the bank to pay your bills.

A forecast can also help you budget for large equipment purchases or identify the need for any loans well in advance, allowing you time to obtain the best rates and deals available.

It allows you to run potential scenarios to predict their impacts on your business's performance. The success of major events such as hiring, expanding or business acquisitions are reliant on the cash available. A cashflow forecast will allow you to ensure such projects are executed at the optimal time.

## The benefits

1. Provides you visibility on how your business is performing
2. Allows you to make sound, well thought out business decisions
3. Ensures you don't commit to spending money you don't have
4. Ensures you don't take unnecessary, expensive, short-term finance when cash may be freed up in the near future
5. Sheds light on bad spending habits
6. Identifies areas for growth and improvement
7. Helps you to achieve your financial goals

## What makes a good cashflow forecast?

The best forecasts are comprehensive and realistic!

### Comprehensive expenditure analysis

When preparing a cashflow forecast it's easy to ensure all your bigger expenditure (think rent, taxes, salaries) make it into the report, but an accumulation of those smaller, "insignificant", costs can add up and dramatically change the cash position. Be sure to include all your commitments.

### Focus on payment terms, not invoice dates

Your suppliers will have different payments terms. Whilst it is important to maintain positive business relationships, these payments terms can be utilised by your business to smooth cashflow. When building your cashflow forecast be sure to consider the required payment dates as opposed to when you will purchase goods or services from suppliers.

### Keep predictions realistic

It's always tempting to over or under-estimate income and outgoings when preparing a cashflow forecast, as it is essentially a guessing game. Keeping things realistic, even on the conservative side, will ensure that your business has the best possible chance of success.

### Forecast for various scenarios

There are so many variables to consider when preparing a cashflow report that your actuals will always vary from the forecast. Forecasting for multiple scenarios can help you prepare for any outcome. Try taking an educated guess as base figures and then flexing the forecast for a 10% higher and lower fluctuation in sales and related costs. This will help you plan for best and worst case scenarios.

### Review your actuals!

One of the main reasons a business might abandon cashflow forecasting is that the actuals never tie up with the forecast. This is an opportunity to learn by identifying the areas which varied the most and adjust the next period's forecast accordingly. You will both improve your understanding of the business's cashflows and improve your forecasting accuracy for the future.

We suggest aligning your forecast to your accounting software and/or year end financial statements. This helps to keep things simple and smooth the process of tracking your forecast against actuals.

**The following pages go on to explain our 5 step process to preparing a cashflow forecast.**

## Contact Us

For the latest news and advice please visit our Facebook, LinkedIn and website pages. If you have any immediate questions or if you would like to discuss anything further please contact us via email or give us a call on:

**01483 898 400**

# 5 Step Process

How to prepare a cashflow forecast

# 1. Time frame

First, you need to discover your time frame.  Essentially you want to plan out as far as you can accurately predict. Now this will vary and will be bespoke to you, depending on the size of your business and whether you have predictable recurring sales and costs.

The most common time frames are:

- Monthly
- Quarterly
- Six monthly
- Annually

**TIP:** Where possible, we recommend against forecasting beyond one year (at least at first), as assumptions, no matter how well thought out, inevitably become less reliable the further into the future you look.

# 2. Preparation

Now it is time to prepare your forecast (see last page for example). This is a two-step process, which goes as follows:

### (a) Determine your cash inflows

List out all the cash you have coming in, have one column for each month and one row for each revenue stream. Remember to focus on when cash will be received, not invoiced.

Start with your historic sales cash inflows from your accounting software and split by sales type. If this varies, focus on the historical and seasonal patterns of your business.

Next include all non-sales income, this could include tax refunds, grants, shareholder investment and royalties, for example.

Now factor in your expectations for additional revenue (new clients, average monthly growth) and extrapolate this across the months in your forecast.

### (b) Calculate your cash outflows

Now that we know what's coming in, let's determine what's going out.

In a similar fashion to determining your cash inflows, use your accounting software to review monthly costs which are fixed and consistent. The most common expenses here will be rent, salaries, loan repayments and tax bills.

Next consider your direct cost of sales. These may well also be fixed if you're a service company with high wages and little other direct costs. If you're in manufacturing on the other hand, we would expect to see cost of sales varying in line with sales. If you have forecast your sales with growth and new client expectations in mind, set up the costs to fluctuate in line with these.

Now factor in all your other expenditure. Start by using an average of actuals over the last year and adjusting for any expected increases or decreases. Next include costs relating to any plans which are not typical running costs, including new marketing strategies, equipment purchasing or additional hiring campaigns for example.

**TIP**: If you are just starting your business and don't have any financial data to review, make sure to use projected revenue and costs. For example, if you have signed a lease for office space, use the monthly rent you will pay moving forward.

**Historic cash inflow**

**+**

**Expected/desired increase/decrease**

**=**

**Forecast income**

**Historic cash outflows**

**+**

**Expected/predicted increase/decrease**

**=**

**Forecast expenditure**

## 3. Insight

By adding up all the figures in your cash inflow rows and taking off the cash outflows for each month, you will arrive at your expected net cashflows for the foreseeable future. Including your bank balance at the beginning of the month can give you a better idea of what cash you have to work with. A running total along the bottom (bank balance at the end of the month) should give you a good indication of your expected cash available over time..

A lot of positive months might signal that you have cash free to either save, invest, or expand your business. On the other hand, consistent negative months may be a stark warning of things to come. We can help you identify ways to increase cashflow such as improved debt collections and using supplier payment terms to your advantage.

## 4. Tracking

Now you have prepared your forecast and considered your actionable changes (Insight), it's time to compare these against your actuals – we call this stage Tracking.

First, record your business's actual cash inflow and outflows during the forecast period on your accounting software. Now calculate the difference between your forecast amounts and your actual results.

Armed with Tracking, you can now track how you are spending your money, what needs to change, and if you're sticking to your financial goals.

**TIP:** Ask yourself these key questions:

- How did I get on?
- Was I too optimistic or did I miss any significant expenses?
- Am I on track to meet my financial objectives and what can you do better next time to produce a more accurate forecast and improve my results?

## 5. Habit

Aim to track your actual results against your forecast at least every quarter, this will help you to create a Habit.

Putting in the work to create your forecast may seem like a hassle, but whilst it takes a bit of time and energy, it's worth the extra effort. Thorough business forecasting gives you the financial insights you need to make the right decisions for your business to grow, scale, and prosper in the future.

# Cashflow Forecast example

Below is a very simple example of what a cashflow forecast will look like and how the first 4 steps of the 5 step process are used to create a forecast.

## 1. Time Frame

Monthly, quarterly, annually?

## 2. Preparation

Determine your current month forecast inflows and outflows using your prior month actual results as a start and then take into consideration any expected/desired/predicted increases and decreases.

| MONTHLY FORECAST | Prior month actuals | Month 1 forecast | Month 2 forecast | Month 3 forecast |
|---|---|---|---|---|
| **Opening bank balance** | **£0** | **£3,500** | **£6,000** | **£10,250** |
| **CASH INFLOWS** | | | | |
| Sales | £5,000 | £10,000 | £15,000 | £50,000 |
| Business loan | £20,000 | £0 | £0 | £0 |
| **CASH OUTFLOWS** | | | | |
| Rent | £2,000 | £2,000 | £2,000 | £2,000 |
| Salaries | £10,000 | £10,000 | £10,000 | £10,000 |
| Marketing | £2,000 | £2,000 | £2,000 | £2,000 |
| Loan repayment | £0 | £500 | £500 | £500 |
| Equipment | £2,500 | £0 | £0 | £2,500 |
| Other outgoings | £5,000 | £5,000 | £4,750 | £4,750 |
| **Closing bank balance** | **£3,500** | **£6,000** | **£10,250** | **£18,000** |

## 3. Insight

Review your closing bank balance. Are you making a cash surplus? Do any of the figures need adjusting? Does it look realistic? Should you hold off making any large purchases?

## 4. Tracking

Compare your forecast to your actual month results. How did you do? Where can you improve?

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