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CASH IS KING – How to prepare a Cash Flow Forecast

By Brad Callaghan

One of the hardest things to do is prepare a Cash Flow forecast for a business that has just started with little or no sales and not knowing what tomorrow holds.

The main reason we should prepare a cash flow forecast is that, we as business owners tend to focus on the bottom line, being the Profit we are going to make. However, we can have \$100,000 in profit but have an overdrawn bank account, this is because we have not managed our cash flow. Now our cash may be tied up in stock or debtors but that is why we should prepare a cash flow forecast and update it weekly until your business has entered into its second year upon which point you have a full year of records to look at. Some of the benefits of a cash flow forecast are below: -

- A forecast can enable you to meet seasonal commitments and plan for future expenditure, e.g. on equipment.
- A cash flow forecast can show when additional funds might be required in both the short and long term.
- Cash flow problems often catch small business owners unaware a forecast will guard against this.
- A careful forecast can help show cash flow patterns in your business.
- The long-term survival of a business depends on its ability to successfully manage cash, and cash flow forecasting and analysis can help with this.

To begin with our forecast will be driven by assumptions and therefore for this forecast to be useful our assumption must be appropriate to our specific industry or business. As I said the second year will be much easier as we have past performance to rely on but the first year we will have to turn to industry stats, benchmarking, dealings with customers and supplies and any knowledge that you may have on the industry.

Some of the main items to focus on will include the following: -

- Sales growth estimates
- If your business/product is seasonal
- Expense that you will incur
- The timing of price increase, from you and your supplies
- To provide for CPI each year, always assume high CPI

Always list your assumptions within the forecast to show how you derived your figures and it will always serve you well when assessing actual performance against forecast.

Now to bring it all together.

Prepare anticipated sales income

Sales can be difficult to predict, and if you are in your second year the best place to start is to look at sales in previous years to identify trends. However if in your first year you will need to rely on realistic estimate based on industry benchmarks and information we mention above. You can also look to identify external and internal items that may affect prices within the first year and adjust accordingly. Now we have determined a sales figure we have to look at the break down of how that money will be received and how much of that will be caught up in debtors. If we assume that, say 70% of debtors will be received within trading terms and 25% outside terms with the remainder 4% to come thereafter and a 1% provision for bad debts. Yes, most businesses will have these so assume and provide for them so they are not a surprise. This should also be included in our list of assumption so we know when time comes to compare.

Cash Inflows and Outflows

To complete our cash flow, we need to prepare a list other incomings and outgoings. Some examples of these include:

- GST refunds and tax refunds
- Government assistance – Diesel fuel rebate; apprentice payments etc
- Dividends received
- Interest received
- Insurance payouts

Outflows

These should include direct and indirect expenses. Some examples of these include:

- Expense necessary to run the business.
- Cost of materials
- Wages & Salaries
- Car/loan repayment
- Payment to any supplies
- New equipment needed
- Fees and charges
- Superannuation payments
- Insurances etc

Always remember that cash is king.

Brad has more than 9 year's professional accountancy experience. Brad has worked in senior management roles within Taxation and Business Services dealing with a number of clients from a range of business sectors. Brad is an avid property investor and renovator and has always been involved in small business ventures since the age of fourteen. Callaghan Partners was formed to deliver and exceed our client's expectations; the continuation of this is the driving passion and focus of our business. Brad enjoys developing his own business interests and property portfolio along with his interests in golf, horseracing and fishing. Brad Can be contacted at www.callaghanpartners.com.au or brad@callaghanpartners.com.au

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