How to master your cash-flow forecast

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Introduction

A cash-flow forecast is fundamental to all businesses. It will help you predict any challenges and proactively respond to changing market conditions.

Your forecast is built on a set of assumptions and shows you how changes in your business will lead to various scenarios – both positive and negative. Many of these assumptions will be based on historical events like patterns of trading or upcoming expenses.

Ultimately, your cash-flow forecast will show you whether your business can meet expectations. By comparing your actual income and expenses with your forecast you'll be able to see which areas are under (or over) performing and react as necessary.

This guide will show you how to get started with your forecast and how to use it.

How to start your cash-flow forecast

For this guide, we'll look at building your own cash-flow forecast using Excel. Most accounting software will have the ability to build one too. Your bookkeeper or accountant will be best placed to help you set that up.

Across the top of an Excel spreadsheet, list time going forwards in whatever time-frame works for you - days, weeks, four weeks or months, for example. It's your choice. If you're using the cash flow to manage your business then weekly and in some cases daily is necessary. If you're looking ahead over a longer time period, then monthly or four-weekly might be better.

On the left-hand side of the spreadsheet, you're going to first list out the different types of income that your business has, then leave a few lines and list the expenses. This will give you a list of the ins and outs. Read on to see exactly what to include.

If you do use a spreadsheet, please check that any calculations within the spreadsheet are correct and that they add the correct range of figures.

What to include

Rolling bank balance

Above the income for the first day or week (depending the time-scale you're using) add your business' available cash balance. At bottom of that column, underneath all of the expenses, leave some room for totals. These will show you the available cash balance at the end of that time period.

There's more on totals at the end of this section.

Income. Your estimated sales

To keep this simple, you can break down your estimated sales into income types - by product or service or by customer, for example.

It's important to remember that your forecast is only as good as the information you put into it, so try to get the detail in here.

Look at your sales history for the last few years and then make various assumptions on how current and future trading conditions will affect these.

Once you've input your sales forecasts, you need to add when you expect payments to be received. Assume most payments will be late (on average two weeks late as a starting point).

Expenses. You estimated costs

Expenses are often grouped into fixed and variable costs.

Fixed costs such as wages and rent will not alter regardless of how much income you're generating. Add dates and anticipated amounts including all bills, fees, professional memberships.

Variable costs such as stock or raw materials will depend on your sales levels. Another variable cost could be how much marketing activity you're doing.

If you can, group these items together in order of flexibility. That will make it easier to focus on the costs that you have control over in the short-, medium- and long-term. Please see the section on **deferred payments** below for more details on this.

Tax and HMRC

If your business is VAT registered, money coming in and going out will usually include VAT. A cash-flow forecast can be more useful if the VAT part is split away from income and expenses. This will make clearer what needs to be put aside to pay your VAT.

The date of the upcoming payment to (or receipt from) HMRC for VAT should also be a separate row on the spreadsheet showing when it will be paid or received. Make sure you add this row to the relevant section - either income or expenses.

You also need to include payment or refunds of other taxes, including PAYE, National Insurance and CIS. Again, these need to go in income or expenses.

Paying senior management

If your company is paying dividends, they are payments from profit and so Corporation Tax will need to be paid on that profit in the future. You may choose to put some money aside each month so that the cash is there to pay Corporation Tax when it's due. This can go in a separate row, as you did with your VAT.

If your company is deemed insolvent, it should not be paying dividends. There is a risk that those dividends could need repaying in the event that the company ends up in an insolvency process.

Deferred payments

Most suppliers to a business would prefer to get a deferred payment rather than no payment at all, so they're often open to discuss reasonable terms. If you can, try to negotiate an alteration to these terms before the payments become overdue.

If a payment has been unavoidably missed, make sure you confirm whether that payment will need to be made and when it must be made by.

If you do agree terms with a creditor, especially HMRC, it's incredibly important that you stick to them or your credibility will be lost. Working out what you can realistically pay, with the help of your cash-flow forecast, will help you negotiate terms that you can stick to.

These future payments will need to be part of your cash-flow forecast.

Combining income and expenses

Add in some totals after income and after expenses. It could help to add totals to each group of income and expenses. This will help you see where your biggest ins and outs are - and help you think about what you can do to change that if you need to.

You'll also need to create totals at the end of each time period. This is then the starting figure for the next period, and so on.

If you give credit to some customers or are given time to pay by one or more suppliers then move them so they're added into the cash flow for the period when they'll be paid, rather than when the sale or purchase took place. This is the main difference between a profit and loss account, which is static, and a cash-flow forecast, which shows real-time cash movement as a result of activities by your business.

TIP: Link cells together to add flexibility to your cash flow forecast.

The more the spreadsheet is linked together, the easier it will be to update and test out different payment and performance positions. Putting a link between cells means that when data changes it's automatically updated across these cells.

If you feel comfortable with Excel or know someone who can help you, creating a series of links for your company information will make it far quicker for you to test different scenarios.

Make sure you check that any links between cells and sheets are accurate. If you can it's an excellent idea to lock cells to prevent them from being changed by accident.

How to use it

Once your cash-flow forecast is in place you can begin to test different payment structures, staffing levels, sales levels and pretty much anything else that crosses your mind.

This cash-flow forecast can now play a big part in your business planning and monitoring as you go forwards.

Of course, your business will change. So it's important to change the forecast too, as the reality moves away from what was forecast. For example, a customer pays their invoice later than expected or sales are greater than expected, which means that a payment to a supplier is forced back or bought forwards.

An effective forecast will manage your cash flow, rather than responding to it.

If you'd like some help creating your cash-flow forecast, or dealing with any of your other business challenges, we offer a free consultation with our business experts. Call 01455 555444 or email us at enquires@fasimms.com to book an appointment.