



Cash Flow

Cash flows are the net amount of cash and cash-equivalents being transferred into and out of a business. Cash received are inflows, and money spent are outflows.

At a fundamental level, a company's ability to create value for shareholders is determined by its ability to generate positive cash flows, or more specifically, maximize long-term free cash flow or FCF. Free cash flow is the cash that a company generates from its normal business operations after subtracting any money spent on capital expenditures.

Successful business owners understand the concept of positive cash flow and maintaining a certain amount of their assets in a liquid form to ensure there is enough cash available to cover monthly expenses, as well as to cover any unexpected expenses.

A liquid asset is an asset that can easily be converted into cash within a short amount of time. Liquid assets include things like cash, money market instruments, and marketable securities. Both individuals and businesses can be concerned with tracking liquid assets as a portion of their net worth.

Inflows are hard to predict and are directly related to contracts and/or sales. Outflows are easier to predict and prepare for, not that there could not be unexpected expenses, but in general we know what they are. Rent, insurance, and utilities are for the most part fixed monthly amounts. We need to understand what our normal outflows are so we can target what our inflows need to be in order to be successful in our business. Budgeting is essential for this process to work well, and the first thing to do will be to determine our outflows.

In order to determine the amount of cash needed for a month, you must first understand what your monthly expenses are, don't forget any annual expenses you may have, these need to be accounted for as well.

Once you know your monthly expenses, calculate your weekly expenses. This will help you achieve your overall goal, as you will be able to work in smaller increments.

We recommend creating internal sub-accounts within your ledgers, you should at a minimum have the following sub-accounts created:

- Operational Expenses. At least 90 days should be accounted for here.
- Emergency Cash. At least \$1,000.00 should be placed in this sub-account.
- Indispensable Equipment replacement fund. This amount will vary from business to business, if you depend on expensive equipment plan for the replacement cost of equipment that is indispensable to your operations and set that amount as a goal to save for.

These sub-accounts should be part of the liquid assets of your company. An asset is considered to be liquid if you can readily convert it to cash, such as a demand deposit (checking account), a savings account is not considered to have liquidity as the bank may require an advance notice to withdraw funds from these accounts.

Not all companies may be able to readily place the required funds into these sub-ledgers, if this is the case, create a plan to periodically add to these sub-ledgers, for example:

- First week of the month move \$200.00 to the Operational Expenses account.
- Second week of the month move \$50.00 to the Emergency Cash account.
- Third and Fourth week of the month move \$500.00 to the Indispensable Equipment Replacement account.



Expenses Example:

Description	Amount
Annual Expenses	
Software license	575.00
Domain registration	350.00
TOTAL ANNUAL EXPENSES	925.00
Monthly allocation for annual expenses (Total divided by 12)	77.08
Monthly Expenses	
Utilities	120.00
Rent	450.00
Insurance	40.00
Website	25.00
Marketing	200.00
TOTAL MONTHLY EXPENSES	835.00
Monthly Expenses Annualized (Monthly Expenses times 12)	10,020.00
Total Annual Expenses	925.00
GRAND TOTAL ANNUAL EXPENSES	10,945.00
Weekly Expenses (Grand Total Annual Expenses divided by 52)	210.48

From the sample chart above we can determine that we need to generate at least \$1,000.00 per month to cover our most basic expenses, not the best scenario by any means since this will not leave any cash for the owner or for any other expenses that may occur. The recommended goal would be to generate inflows that are one-and-a-half times the size of our outflows.