

Cash is King

by

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Cash is king, as the old saying goes. It is the one resource a company cannot survive without for any length of time until the doors are closed, voluntarily or involuntarily, which is why the **CEO** must find or develop a method to reliably understand and predict the company's current and future ability to generate the cash it needs to pay all of its bills.

Forecasting cash flow is much easier than it used to be, thanks to the convenient number-crunching power of PCs and spreadsheet software which allows one to build an **Integrated Spreadsheet** which links a projected balance sheet and income statement for the business. The Integrated Spreadsheet is a tool that will give any CEO the positive direct control they must have over the financial rudder of the business.

A wise time investment for CEO's

A company's cash flow at any point in time is a juxtaposition of payables, receivables, debt service, capital expenditures, sales/repurchases of stock, and other factors. An Integrated Spreadsheet handles this complex financial interaction with electronic precision. Using this tool, a CEO can more carefully predict where the company is heading. That's powerful planning and peace of mind for the executive/owner that shoulders the burden of consistently meeting payroll and staying current with suppliers on all bills.

- The Integrated Spreadsheet gives the CEO a rational way to appropriately pace capital expenditures, quarterly (or even monthly) bonus payments, and sweeps of excess cash into less liquid but higher-returning financial instruments at the earliest possible time.
- The Integrated Spreadsheet allows the CEO to look at the effect on cash from big-picture business initiatives such as acquiring a new business, selling off a division, developing and staffing a new department, or launching a new product line.
- Using an Integrated Spreadsheet helps the CEO disclose mistakes that are sometimes made in monthly financial statements from either miscoding or a faulty accounting interpretation of a particular transaction.
- With an Integrated Spreadsheet the company always has a three-year plan that is built on actual operating numbers, but fine-tuned to reflect management's best judgment of future revenues and expenses.
- The Integrated Spreadsheet can easily generate an unlimited number of graphs to analyze past performance and predict future performance which is often the most effective way to communicate financial data to employees, directors, shareholders, and the bank.

- An Integrated Spreadsheet will demonstrate to the bank, board, and investors that the financial management and budgeting of the company is under control which promotes confidence in the officers and the business by its internal and external constituents.

DIY

Assuming the user knows their way around a spreadsheet and double- entry accrual accounting, the structure of an Integrated Spreadsheet can be set up in a few hours. It will take a day or so to input the previous twelve months of operating data; a day to input informed estimates of revenues, expenses, and capital expenditures for the next twelve months and to fine-tune those estimates; and a day to train all users who will have access to the Integrated Spreadsheet.

If the CEO cannot spare the time, this task can be delegated to inside accounting staff or subcontracted to an outside accountant or consultant. If this project is delegated, it is still important that the CEO be trained in the use of the Integrated Spreadsheet so that he or she can perform what-if analyses and generally watch over the constantly revising forecast of the financials of the business, a function that should be owned by the CEO. Financial forecasting involves hundreds of experience-based estimates of highest-probable outcomes of revenues, expenses, capital expenditures, debt service, equity inflows and outflows, extraordinary gains and losses, and other income and expenses, by someone that has the overview of the business. The CEO has this overview as it is part of the responsibility of the position.

Basic structure of the integrated spreadsheet

It is important for the user to have a general understanding of how the spreadsheet is laid out and functions. The integrated spreadsheet has three major components:

- Balance Sheet
- Income Statement
- Cash flow adjustment

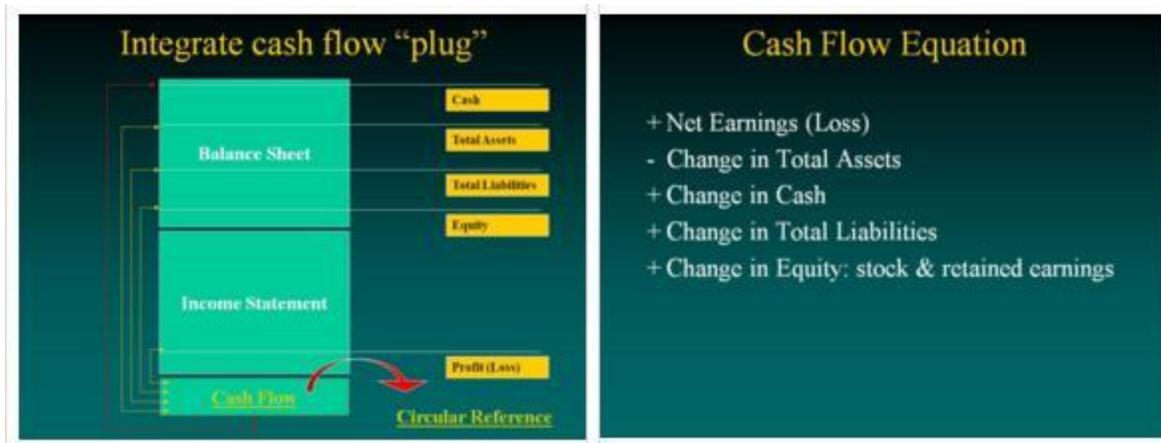
These three components are linked or integrated so that they balance or tie out in accrual accounting terms. These integrated accounts are highlighted in various colors as shown on the diagram below:

A	B	C	D	E	F - L	M	N	O	P	
1										
2	BALANCE SHEET	Beginning Balance	Jan	Feb	March	April-Oct	Nov	Dec	Total Change	Ending Balance
3	Current Assets									
4	Cash & equivalents	1,000	38,010	38,010	38,010	~	38,010	38,010	456,120	457,120
5	Accounts receivable	100,000	1,000	1,000	1,000	~	1,000	1,000	12,000	112,000
6		101,000	39,010	39,010	39,010	~	39,010	39,010	468,120	569,120
7	Long Term Assets									
8	Property & Equipment	20,000	2,000	2,000	2,000	~	2,000	2,000	24,000	44,000
9	Less accumulated dep	(1,000)	(1,000)	(1,000)	(1,000)	~	(1,000)	(1,000)	(12,000)	(13,000)
10		19,000	1,000	1,000	1,000	~	1,000	1,000	12,000	31,000
11	TOTAL ASSETS	120,000	40,010	40,010	40,010	~	40,010	40,010	480,120	600,120
12										
13	Current Liabilities	3,000	5,000	5,000	5,000	~	5,000	5,000	60,000	63,000
14	Long Term Liabilities	1,000	1,000	1,000	1,000	~	1,000	1,000	12,000	13,000
15	TOTAL LIABILITIES	4,000	6,000	6,000	6,000	~	6,000	6,000	72,000	76,000
16										
17	Stockholders' Equity									
18	Paid-in-Capital	1,000	1,000	1,000	1,000	~	1,000	1,000	12,000	13,000
19	Profit (loss)		33,010	33,010	33,010	~	33,010	33,010	396,120	396,120
20	Retained Earnings	115,000	0	0	0	~	0	0	0	115,000
21		116,000	34,010	34,010	34,010	~	34,010	34,010	408,120	524,120
22	TOTAL LIAB & EQUITY	120,000	40,010	40,010	40,010	~	40,010	40,010	480,120	600,120
23										
24	INCOME STATEMENT									
25	Revenues		100,000	100,000	100,000	~	100,000	100,000	1,200,000	
26	Operating Expenses									
27	All other expenses		65,990	65,990	65,990	~	65,990	65,990	791,880	
28	Depreciation expense		1,000	1,000	1,000	~	1,000	1,000	12,000	
29			66,990	66,990	66,990	~	66,990	66,990	803,880	
30										
31	PROFIT (LOSS)		33,010	33,010	33,010	~	33,010	33,010	396,120	
32										
33	CASH FLOW									
34	- Change in ASSETS		(2,000)	(2,000)	(2,000)	~	(2,000)	(2,000)	(24,000)	
35	+ Change in LIABILITIES		6,000	6,000	6,000	~	6,000	6,000	72,000	
36	+ Change in P-I-C & RE		1,000	1,000	1,000	~	1,000	1,000	12,000	
37	Cash Flow >>>		38,010	38,010	38,010	~	38,010	38,010	456,120	

The major points of integration are identified by the matching colors. For example, the link between “depreciation” on the balance sheet and “depreciation expense” on the income statement is shown in brown, since these two entries must be identical in double-entry accrual accounting. There are in fact numerous links between the income statement and the balance sheet as a result of the double-entry methodology. The beauty of the spreadsheet is it affords the user the flexibility to add/subtract/modify at will and build increasing sophistication into the integrated spreadsheet enabling a more realistic modeling of the financial dynamics of the business.

I’ve posted a [power point presentation on prezi](#) that leads you through the basic construction of the integrated spreadsheet. The secret sauce in this process is the synching of a cash flow

adjustment (plug) at the bottom of the spreadsheet below the income statement as shown in the diagram below:



By wiring together these key accounts to calculate the actual cash flow for each month, this will cause what's known as a circular calculation in the spreadsheet which is normally a no-no, but in this case it is a good thing! The user simply needs to go into "settings" and set the automatic calculation to 100 iterations and the spreadsheet will automatically recalculate and balance the statements after each new value entry to a cell.

Using the tool

Once the integrated spreadsheet is set up, using it effectively involves inputting the actuals from each monthly financial statement as they occur and reforecasting the numbers going forward from the most recent actuals. This process repeats itself every month — inputting the most recent actuals and reforecasting ahead — and as each month goes by and the user gains experience in using the spreadsheet and making experience-based judgments of how the numbers will track, the integrated spreadsheet becomes an expert system that does a better job over time of forecasting the financial fortunes (or misfortunes) of the company. The key point is that all of this boils down to one most important account: **cash flow**.

Once the process of updating actuals and forecasting ahead is complete, the CEO looks at the impact on cash and then develops a financing plan that optimizes the uses of working capital in the next six months and beyond.

If the projected cash flow shows surpluses being generated, the CEO can decide how that excess cash could be used today and in the coming months to:

- Reduce payables
- Reduce long-term debt
- Make capital expenditures
- Make other long-term investments

If the projected cash flow is negative, the CEO must plan for how the minimum working capital requirements for the business will be generated to carry the company through tight cash periods by a combination of:

- Drawing down cash surpluses
- Deferring certain operating and capital expenditures
- Extending the payables cycle for a brief period within acceptable bounds
- Making a draw on an operating line of credit
- Securing additional long-term financing
- Raising equity capital through the sale of common or preferred shares

Summary

If the CEO can build the integrated spreadsheet for the business and start using it each month (if not each day), learning by doing is the most efficient user's manual. The CEO will quickly discover the many dimensions of value that are derived from the integrated spreadsheet aside from the very tangible value of forecasting cash flow. The integrated spreadsheet causes the user to think about every aspect of the business, across all accounts, across time, across strategies, by looking back to look forward. And at the end of the exercise instead of saying, "I hope we'll have the money in the bank when we need it," the CEO can say, "We expect to have the cash we need, and here's how."

That's powerful business confidence!