



Brief #04.05

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Projected Financial Statements

Projected Financials Statements are a best estimate of a firm's future financial position. Testing the assumptions behind these statements is a critical part of developing your business plan, evaluating your product/service costs and profitability, and estimating your cash requirements.

SCORE Business Brief [Excel 1200.xls](#) is a spreadsheet tool that will let you create these statements. Excel formulas generate the projected statements based upon your data entry of:

- forecasted unit sales by product line
- unit selling price, direct labor and material, gross profit by product line
- monthly budget for overhead (selling and administrative) salaries and operating expenses
- sources of operating capital: equity from owners and debt financing from outside lenders
- initial funds required for startup costs, including building space and equipment
- time required to collect accounts receivable, schedule of debt repayments

Detailed instructions on using Excel 1200 are located on the first two tabs of the spreadsheet and account descriptions/examples are provided throughout .A background discussion of the business purpose of each statement follows:

Income Statement

The Income Statement provides a systematic method of recording sales, cost of goods sold, and expenses and deriving the profit or loss resulting from business operations. The Income statement is often referred to as the Profit and Loss (P&L) statement.

Expenses include such items as wages and benefits, advertising, rent, utilities, insurance and taxes. For a business using the accrual method of accounting, additional entries must be made for accruals for payroll and other taxes, insurance, and the like. For a business using the accrual method it is highly recommended that an accountant be used to handle the books.

The Income Statement also forms the basis for generating cash flow projections. It differs from the Cash Flow Statement primarily by including non-cash tax deductible expenses such as amortization, depreciation and provisions for inventory losses and bad debts. The Income Statement does not include non-deductible expenditures which affect cash flow. Some examples of these expenses are pre start-up costs, purchase of capital equipment, payment of principal on loans, dividends and distributions to owners, and cash infusions, such as from sales of capital stock and/or loans or additional investments from the owners.

Unit Sales/Sales Price Forecasting

Before an Income Statement can be completed and a pricing structure established, it is necessary to know or to estimate various important factors of the business, for example: What are the variable costs (i.e., those dependent on unit sales) to provide the product or service? What are the fixed costs of just being in business? At what sales level does the business at least break even? At the projected sales level, does the pricing allow the business to operate at a reasonable profit and still remain competitive?

The statement should also provide for comparing estimated and actual sales, and expenses and profit as they become known. The format should be adapted to the particular business for which the projection is being made, with appropriate changes in the entries as may be required.

The sales forecast is probably the most difficult part of the business to estimate – especially for a starting business. Learn more at Brief 06.04, Sales Forecasting.

Balance Sheet

A balance sheet, also known as the "statement of financial position", reports the assets, liabilities, and stockholders' equity (net worth) of a business at a specific date, usually at the close of an accounting period. This financial statement details:

Assets - the nature and amounts of enterprise resources

Liabilities - the claims of creditors against those assets

Owners' Equity – ownership's net resources from stock purchases + retained earnings

The components of the balance sheet must equal (or balance out) so that:

$$\mathbf{Assets = Liabilities + Owners' Equity (net\ worth)}$$

The balance sheet provides a basis for:

- ✓ evaluating the capital structure of the business
- ✓ computing rates of return on that capital structure
- ✓ analyzing liquidity – the time required to convert assets into cash to pay bills
- ✓ analyzing solvency – the ability of the business to pay debts as they become due
- ✓ measuring the value of the business to interest partners to invest in the business

Refer to SCORE Business Brief 4.11, Key Financial Ratios, for key analytical measures of business health that can be calculated with balance sheet values.

A business with growing sales will need increased operating assets such as accounts receivable and inventory and may need more equipment and space. Funding this expansion may come from increased accounts payable (an indirect form of supplier financing), additional shareholder contributions (stock purchases or loans), retained earnings, or use of a line of credit from a bank.

Cash Flow Statement

Cash Flow Statements and Projections are statements and predictions of inflow and outflow of **cash only. Only cash will pay bills**, and if you can't pay your bills you'll be out of business.

The Cash Flow Projection will also serve as an early warning indicator when your expenditures are running out of line, or your sales targets are not being met. As the manager of your cash, you will have enough time to devise remedies for anticipated temporary cash shortfalls and ample opportunity to arrange short term investments for the business' temporary cash flow surpluses.

The completed cash flow forecast will clearly show to a bank loan officer (and you) what additional working capital, if any, the business may need, and will offer proof that there will be sufficient cash on hand to make the interest payments to support a revolving line of credit (to cover the shortfalls), or a term loan for major purchases.

These projections become more useful when the estimated information is compared with actual information as it develops. Utilize cash flow projections to assist in understanding how your business is doing compared to the plan and why, and for setting new goals, and planning operations for more profit.

Much of the data to project your cash flow is the same as, and can be obtained from, the income statement. The main differences are that the Cash Flow statement includes non-tax-deductible expenses such as pre start-up costs, purchases of capital equipment, payment of principal on loans, dividends and distributions to owners, includes cash infusion from sales of capital stock, and loans, but excludes non-cash tax-deductible categories such as amortization, depreciation, provision for inventory losses and bad debts.

The cash position at the end of each month needs to be adequate to meet the cash requirements for the upcoming month. If too little cash is available, then additional cash will have to be injected or cash to be paid out must be reduced. If there is consistently too much cash on hand, the money is not working for your business.

Your cash forecasts you must include taxes you will have to pay. For your own safety, you should never include in your available cash any cash you have collected in sales taxes; sales taxes are not included in your gross sales, and should be put into a separate account to have available when it is time to remit these taxes, usually quarterly.

In addition, it is a good idea to put all the money you collect in Social Security and Medicare, both that withheld from employee payroll as well as the matching company payments, together with federal, state and local taxes withheld from employee payrolls into a separate account until payment is due. This is not your cash, and should not be used to cover business expenses. If you can't pay these amounts when due, the tax collectors will most likely close you down and impose severe penalties.

If you would like to request a SCORE counselor, please [click here](#).

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