Creating a Cash Flow Forecast

My SCORE colleagues and I mentor small businesses that are trying to figure out how to grow their business. One of the first discussion points becomes what is your current cash flow like and what is the potential for the future? In our last few columns I have discussed various aspects of financial management including the cash flow statement. But now we need to take this a step forward and think about how might this picture look in the future.

A cash flow forecast differs from a cash flow statement. While the cash flow statement shows all inflows and outflows of cash that occurred during a particular time period (such as a month or a quarter), a cash flow forecast predicts how cash will move in and out of the business over some future period of time (typically one year).

Using a cash flow forecast can help you predict future sales, understand how profitable these future sales will be, and show you what you need to do differently to achieve your goals. Used correctly, a cash flow forecast forms the basis of your plan for business growth.

Here are some suggestions on how to create a cash flow forecast.

1. Categorize sales by customer type, or product/service type.
2. For each category, identify a transaction type, average price and frequency.
3. Estimate direct costs of producing, selling, general and administrative expenses.
4. If the result is unprofitable or unrealistic, adjust the numbers.
5. From the forecast, identify what you need to do differently to achieve the forecast.

I generally recommend a rolling 13-week cash flow forecast because it covers a full quarter and is forward-looking. The secret to using a 13-week cash flow forecast is reviewing it and modifying it at least once a week. You’ll find that weeks in the near future will be much more accurate in their forecast than those eight to 10 weeks out. However, the more often you use your cash flow forecast, the more accurate you will become in estimating cash inflows and outflows.

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