





# CASH FLOW STATEMENT

# Introduction

- Cash plays a very important role in the economic life of a business.
  - A firm needs cash to make payment to its suppliers, to incur day-to-day expenses and to pay salaries, wages, interest and dividends etc.
  - In fact, what blood is to a human body, cash is to a business enterprise.
  - Thus, it is very essential for a business to maintain an adequate balance of cash.
  - For example, a concern operates profitably but it does not have sufficient cash balance to pay dividends, what message does it convey to the shareholders and public in general.
  - Thus, management of cash is very essential.
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# Cash flow statement

- Cash flow statement provides information about the cash receipts (Inflows) and payments (outflows) of a firm for a given period.
  - It is a statement depicting change in cash position from one period to another.
  - For example, if the cash balance of business is shown by its Balance sheet on 31st December, 2012 at \$20,000 while the cash balance as per its balance sheet on 31st December, 2013 is \$30,000. There has been an inflow of cash of \$10,000 in the year 2013 as compared to the year 2012.
  - It explains the reasons for such inflows or outflows of cash, as the case may be.
  - It also helps management in making plans for the immediate future.
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# Purpose of the Statement

- ❓ To provide relevant information about the cash receipts and cash payments of an enterprise during a period.
- ❓ The statement provide answers to the following questions:
  1. Where did the cash come from?
  2. What was the cash used for?
  3. What was the change in the cash balance?



# Why cash flow Analysis ???

- Its an important analytical tool for creditors, investors and other users of financial statement data.
- ☐ Firm's ability to generate cash flows in the future
- ☐ Firm's capacity to meet cash obligations
- ☐ Firm's future external financing needs
- ☐ Firm's success in productively managing investing activities
- ☐ Firm's effectiveness in implementing financing and investing strategies



# Objectives of Cash Flow Statement

Highlighting cash flow from different activities

Short-term Planning

Cash Flow information helps to understand liquidity

Efficient cash management


Prediction of sickness

Comparison with budget

Cash position



# Cash Flow Statement : Limitations

- Does not show the **liquidity position** of the firm because an income statement takes into account both cash as well as non-cash items
  - It is not a substitute of **income statement**
  - Does not show the **financial position** of the firm in totality
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# Distinction between Cash flow Statement and Funds Flow Statement

## Basis f Difference

## Cash Flow

## Funds Flow

### Basis of Accounting

It recognizes Cashbasis Of accounting

It is based upon accrual Basis of accounting I.e Working capital

### Significance

It is useful for short-Term financial planning

It is useful for long-term Financial planning

### Schedule of Changes in Working Capital

Such a schedule is not Prepared for preparing Cash flow statement

Schedule of changes in Working capital is Prepared separately

### Causes of Variation

It studies only the Causes of cash variation

It studies causes of change in working capital



# Where from: Where to?

Cash comes from

- 1 Profits
- 2 Sales of Fixed Assets
- 3 Decrease in Stock
- 4 Decrease in Debtors
- 5 Capital Introduced
- 6 Loans Received
- 7 Increase in Creditors

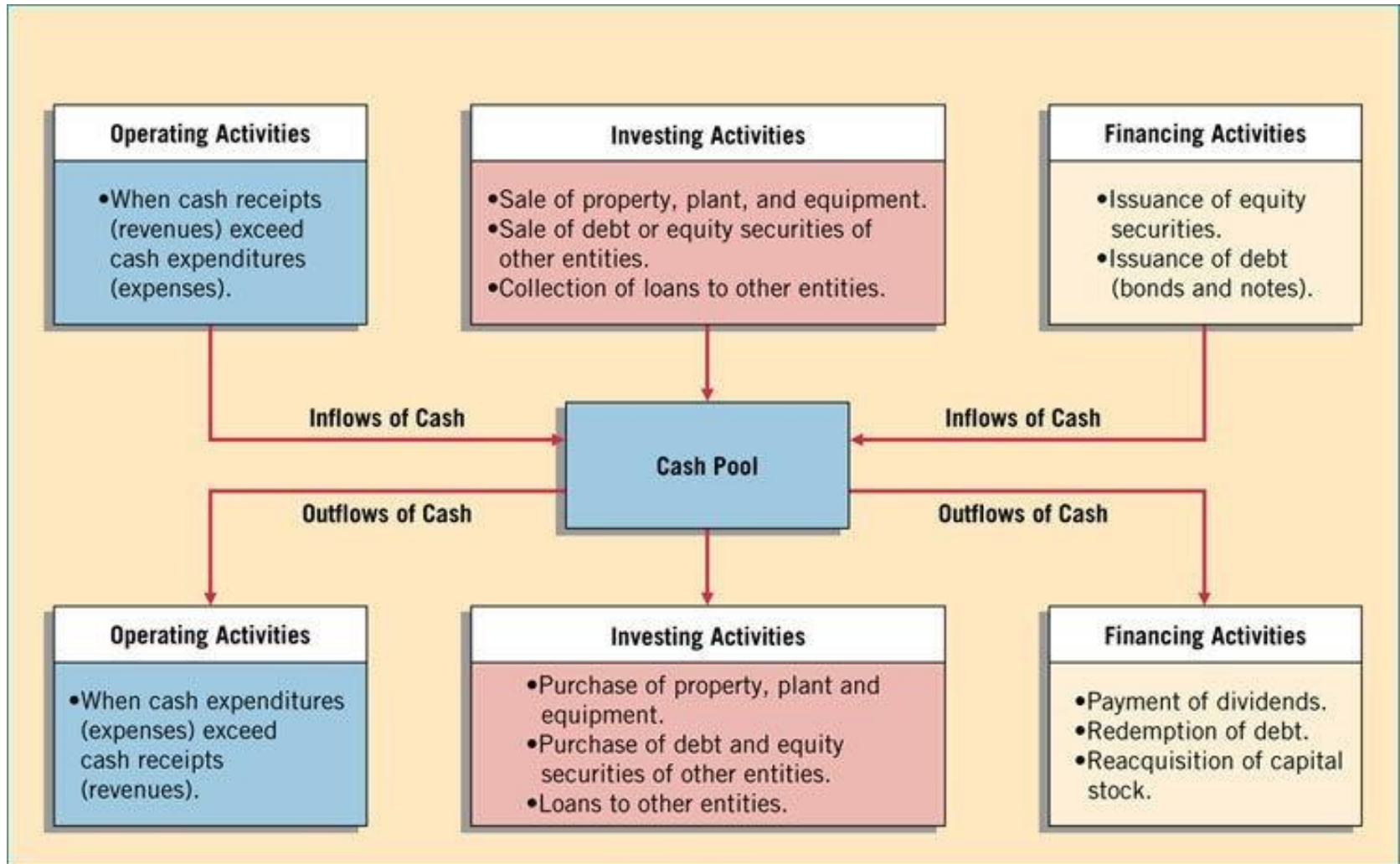


Cash goes to

- 1 Losses
- 2 Purchase of Fixed Assets
- 3 Increase in Stock
- 4 Increase in Debtors
- 5 Drawings/Dividends
- 6 Loans Repaid
- 7 Decrease in Creditors

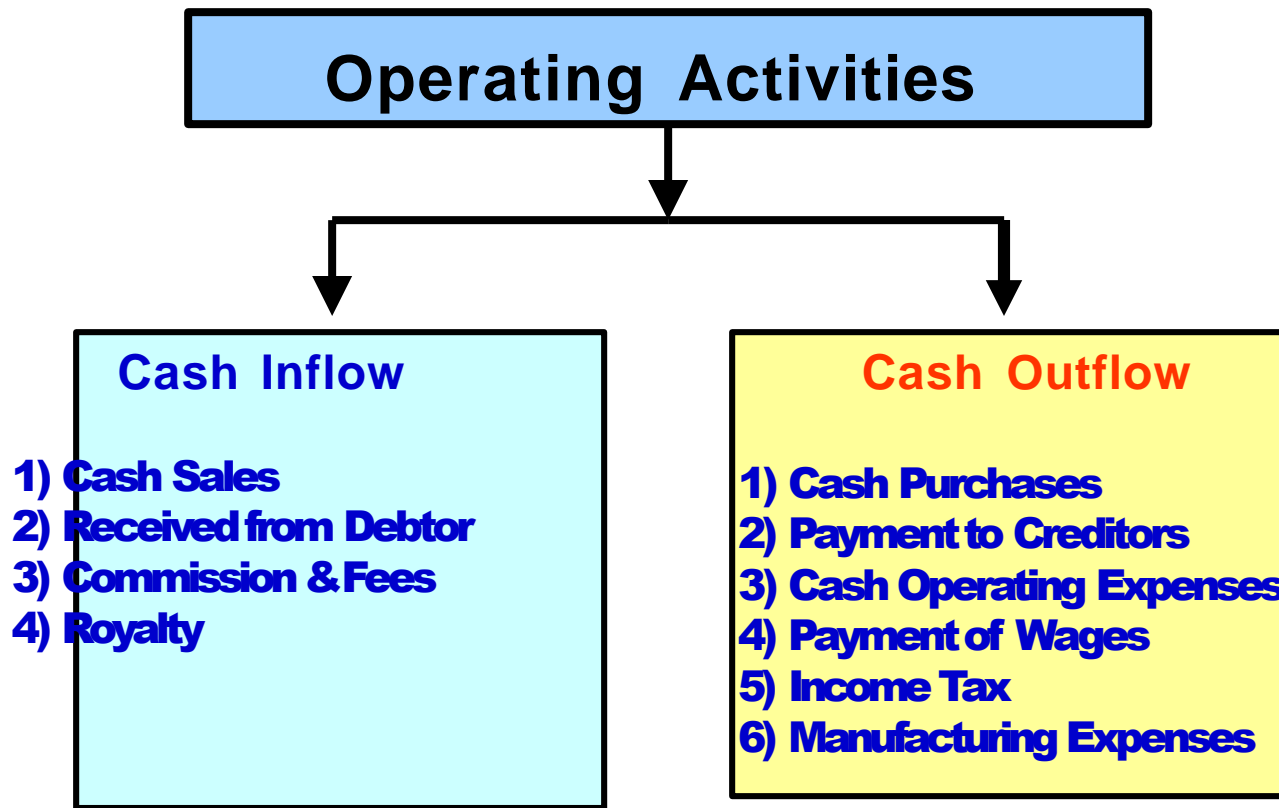


# Classification of Cash Inflows and Outflows



## Operating activities

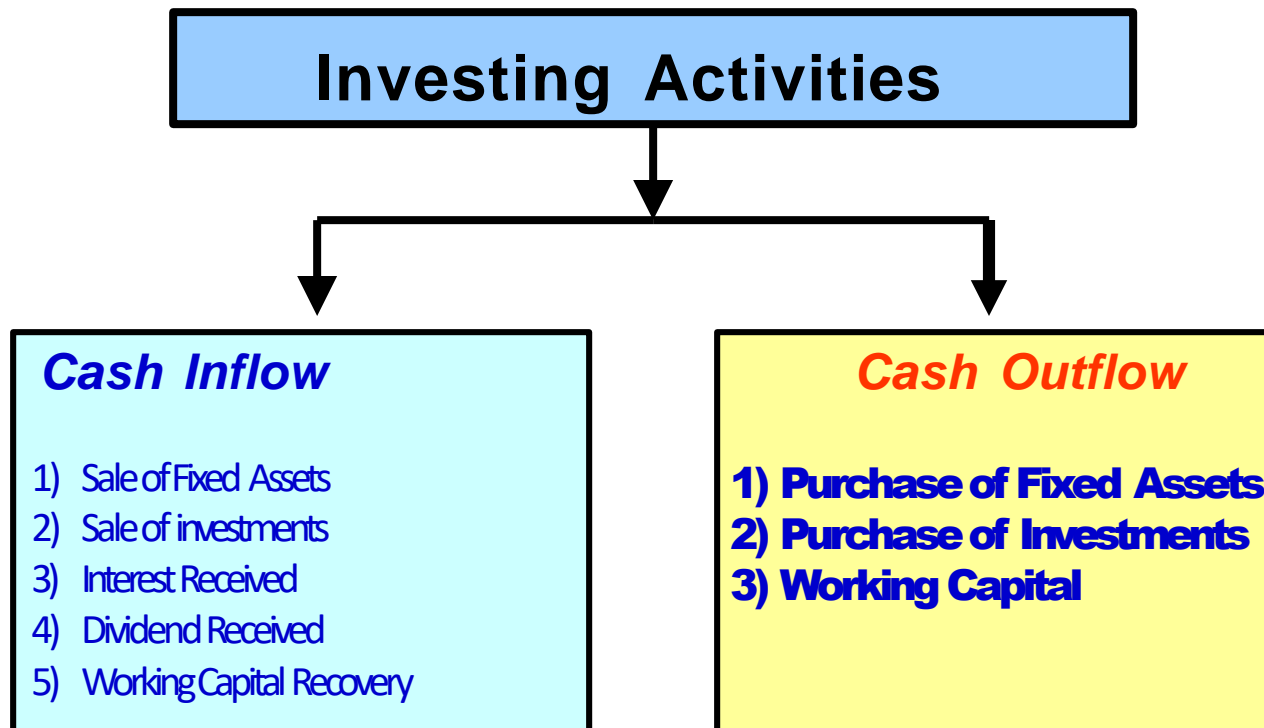
It includes **receiving cash** from customers for the sale of goods and services, receiving interest and dividends on loans and investments, and **making cash payments** for wages, goods and services purchased, interest, and taxes.



Cash effects the transaction on Net Income

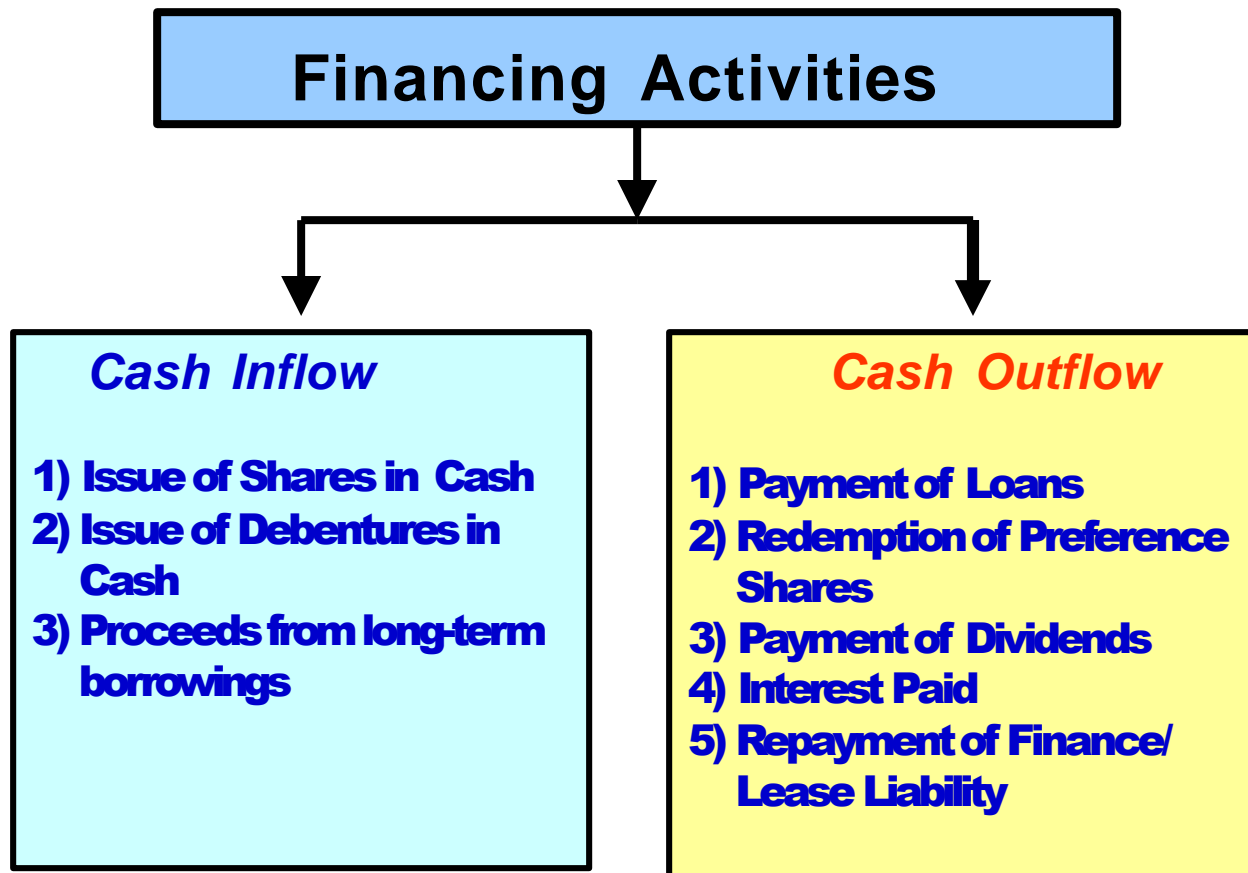
## Investing activities

It includes ***purchasing and selling*** long-term assets and marketable securities (other than cash equivalents), as well as making and collecting on loans.



## Financing activities

It includes issuing and buying back capital stock, as well as borrowing and repaying loans on a short- or long-term basis (issuing bonds and notes). Dividends paid are also included in this category.



The specimen form for computation of cash from operations is given below :

### Calculation of Cash from Operations :

(Combining Current Assets & Current Liabilities & Non-Cash & Non-Operating Items)

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Net Profit (Closing Balance of Profit & Loss A/c)		* * *
<i>Add:</i>		
Depreciation on Fixed Assets	* * *	
Transfer to General Reserve		
Loss on Sale of Fixed Assets		
Loss on Sale of Investments		
Goodwill Written off		
Increase in Outstanding Expenses		
Decrease in Prepaid Expenses		
Decrease in Current Assets (Other than Cash and Bank)		
Increase in Current Liabilities		
Preliminary Expenses Written off	* * *	* * *
<i>Less :</i>	* * *	
Profit on Sale of Fixed Assets		
Profit on Sale of Investments		
Decrease in Outstanding Expenses		
Increase in Prepaid Expenses		
Increase in Current Assets (Other than Cash and Bank)		
Decrease <del>Increase</del> in Current Liabilities		
Opening Balance of Profit & Loss A/c		* * *
<b>Cash From Operations</b>		* * *

**Illustration: 1**

From the following Balance Sheet of ABC Ltd., you are required to calculate Cash From Operations:

<i>Particulars</i>	<i>2002</i> <i>Rs.</i>	<i>2003</i> <i>Rs.</i>
<b>Capital and Liabilities :</b>		
Share Capital	20,000	20,000
Profit made during the year	14,100	17,300
Provision for Depreciation	1,000	1,400
Long-Term Loans	2,000	3,000
Trade Creditors	6,450	5,300
Outstanding Expenses	850	150
	<b>44,400</b>	<b>47,150</b>
<b>Assets :</b>		
Plant and Machinery	28,500	30,000
Stocks	9,800	11,300
Trade Debtors	3,950	2,850
Cash Balances	2,150	3,000
	<b>44,400</b>	<b>47,150</b>

**Solution :**

### Calculation of Cash from Operations

<i>Particulars</i>	<i>2002 Rs.</i>	<i>2003 Rs.</i>
Profit made during the year (Closing Balance of P & L A/c)		17,300
<i>Add :</i>		
Provision for Depreciation	400	
Decrease in Debtors	1,100	1,500
		18,800
<i>Less :</i>		
Decrease in Creditors	1,150	
Decrease in Outstanding Expenses	700	
Increase in Stock	1,500	
Net Profit (Opening Balance of P & L A/c)	14,100	17,450
Cash From Operations		1,350



## Illustration: 2

From the following balance you are required to calculate cash from operations

<i>Particulars</i>	<i>2002</i> <i>Rs.</i>	<i>2003</i> <i>Rs.</i>
Trade Debtors	1,00,000	94,000
Bills Receivable	20,000	25,000
Trade Creditors	40,000	50,000
Bills Payable	16,000	12,000
Outstanding Expenses	2,000	2,400
Prepaid Expenses	1,600	1,400
Accrued Income	1,200	1,500
Income Received in Advance	600	500
Profit made during the year	—	2,60,000

**Solution:**

### Calculation of Cash from Operations

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Net Profit (Closing Balance)		2,60,000
<b>Add :</b>		
Decrease in Debtors	6,000	
Increase in Creditors	10,000	
Increase in Outstanding Expenses	400	
Decrease in Prepaid Expenses	200	16,600
		2,76,600
<b>Less :</b>		
Increase in Bills Receivable	5,000	
Decrease in Bills Payable	4,000	
Increase in Accrued Income	300	
Decrease in Income Received in Advance	100	9,400
Cash From Operations		2,67,200

### Illustration: 3

From the following information given by RR Ltd., you are required to prepare Cash From Operations:

<i>Particulars</i>	<i>2002 Rs.</i>	<i>2003 Rs.</i>
Bills Payable	10,000	16,000
Trade Creditors	24,000	32,000
Outstanding Expenses	4,000	2,000
Bills Receivable	40,000	36,000
Trade Debtors	80,000	1,20,000
Prepaid Expenses	4,000	6,000
Accrued Incomes	10,000	16,000
Incomes Received in Advance	4,000	2,000

### Additional Information

RR Ltd., earned profit of Rs. 4,00,000 after charging or crediting the following items to its profit and loss account during the year 2003:

- (1) Profit on Sale of Investments Rs. 8,000
- (2) Loss on Sale of Building Rs. 18,000
- (3) Depreciation on Fixed Assets Rs. 14,000
- (4) Good Will Written off Rs. 4,000

**Solution:****Calculation of Cash from Operations**

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Net Profit during the year		4,00,000
<b>Add :</b>		
Loss on Sale of Building	18,000	
Depreciation on Fixed Assets	14,000	
Good will Written off	4,000	
Increase in Bills Payable	6,000	
Increase in Trade Creditors	8,000	
Decrease in Bills Receivable	4,000	54,000
		<b>4,54,000</b>
<b>Less :</b>		
Profit on Sale of Investments	8,000	
Decrease in Outstanding Expenses	2,000	
Decrease in Income Received in Advance	2,000	
Increase in Trade Debtors	40,000	
Increase in Prepaid Expenses	2,000	
Increase in Accrued Income	6,000	60,000
<b>Cash From Operations</b>		<b>3,94,000</b>

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