

# How to Make Cash Flow Projections

*By Tim Spilker*

Cash flow projection is the most powerful tool in cash management. It enables you to see the cash flowing in and out of your organization so that you can plan for surpluses as well as deficits.

Essentially, the cash flow projection is a forecast of your organization's cash income and expenditures on a weekly or monthly basis. Preparing cash flow projections is like preparing a budget and balancing your checkbook at the same time. But, unlike your budget, it deals only with cash transactions over a specified period of time.

Your own organization's cash flow projections should be tailored to its specific situation, but the building blocks are the same for all organizations. Using your annual operating budget as the starting point, you begin by identifying each month's anticipated income, then identify each month's anticipated expenditures, and arrive at each month's cash flow. To be effective, your cash flow projections should be updated at least monthly, if not weekly, using actual financial information, such as receipts, checks, bills and account figures. That way you will know what actions you need to take or which expenses you need to monitor in order to ensure that cash flow stays positive.

The chart on this page shows a simple cash flow projection for the first four months of the year. The organization's operating budget is included as the starting point, and its anticipated income and anticipated expenditures are listed for each month. Many of the organization's fixed expenses, particularly payroll and benefits, are consistent for each month. For variable expenses, such as supplies, postage and program expenses, the organization estimated its anticipated expenses, based on historical trends and current information available.

By looking at the operating income or loss (line 1) in our sample cash flow projection, you can see the "peaks and valleys" in the organization's annual cash flow. The operating income or loss (line 1) for each month is calculated by subtracting total expenditures from total income. In our example, the organization has an operating loss of \$13,433 for the month of January: income of \$4,500 minus expenses of \$17,933 = (\$13,433), and an operating income of \$44,417 in April: income of \$67,000 minus expenses of \$22,583 = \$44,417. Your month-to-month operating income or loss is useful in cash

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management because you can see where you will face deficits (in our example, January) and where you will realize surpluses (in our example, April). You can anticipate when these surpluses and deficits will occur well before they happen, meaning that you have ample time to identify strategies for dealing with both.

The next part of the cash flow projection is the beginning cash balance (line 2)—the money available to you in your bank accounts or in cash at the beginning of the month. In our example, the organization started January with \$2,648 in the bank.

When you consider your operating income or loss in relation to your beginning cash balance, you know your cash flow surplus or deficit (line 3), the sum of your operating income or loss and beginning cash balance. For January, the \$13,433 operating loss and the \$2,648 beginning cash balance in the organization's bank account results in a cash flow deficit of \$10,785. However, by the end of April the organization has a cash flow surplus of \$48,015.

### Sample Cash Flow Projection for ABC Stable Nonprofit Organization

|                                 | total<br>budget | jan          | feb          | mar           | apr           |
|---------------------------------|-----------------|--------------|--------------|---------------|---------------|
| <b>ANTICIPATED INCOME</b>       |                 |              |              |               |               |
| interest from endowment         | 4,000           | 1,000        | 0            | 0             | 1,000         |
| government grants               | 35,000          | 0            | 0            | 15,000        | 0             |
| foundation grants               | 100,000         | 0            | 5,000        | 0             | 0             |
| individual donations            | 90,000          | 2,500        | 0            | 2,500         | 65,000        |
| fee for service                 | 20,000          | 1,000        | 1,000        | 1,000         | 1,000         |
| <b>TOTAL INCOME</b>             | <b>249,000</b>  | <b>4,500</b> | <b>6,000</b> | <b>18,500</b> | <b>67,000</b> |
| <b>ANTICIPATED EXPENDITURES</b> |                 |              |              |               |               |
| salary and benefits             |                 |              |              |               |               |
| executive director              | 50,000          | 4,167        | 4,167        | 4,167         | 4,167         |
| program director                | 30,000          | 2,500        | 2,500        | 2,500         | 2,500         |
| program director                | 30,000          | 2,500        | 2,500        | 2,500         | 2,500         |
| development director            | 30,000          | 2,500        | 2,500        | 2,500         | 2,500         |
| administrative support          | 25,000          | 2,083        | 2,083        | 2,083         | 2,083         |

|                                 |                |               |               |               |               |
|---------------------------------|----------------|---------------|---------------|---------------|---------------|
| operating                       |                |               |               |               |               |
| rent                            | 20,000         | 1,667         | 1,667         | 1,667         | 1,667         |
| supplies                        | 8,000          | 1,000         | 0             | 2,000         | 0             |
| telephone                       | 8,000          | 667           | 667           | 667           | 667           |
| postage                         | 6,000          | 500           | 500           | 500           | 500           |
| copying                         | 8,000          | 100           | 100           | 100           | 100           |
| program                         |                |               |               |               |               |
| program expenses                | 25,000         | 250           | 250           | 4,000         | 5,000         |
| <b>TOTAL EXPENDITURES</b>       | <b>240,000</b> | <b>17,933</b> | <b>16,933</b> | <b>23,183</b> | <b>22,583</b> |
| <br>                            |                |               |               |               |               |
| 1 OPERATING INCOME or<br>(LOSS) | 9,000          | (13,433)      | (10,933)      | (4,683)       | 44,417        |
| 2 BEGINNING CASH BALANCE        | 2,648          | 2,648         | 4,215         | 8,281         | 3,598         |
| 3 CASH FLOW<br>SURPLUS/DEFICIT  | 11,648         | (10,785)      | (6,719)       | 3,598         | 28,015        |
| 4 LINE OF CREDIT/LOAN PMT.      | 15,000         | 15,000        | 15,000        | 0             | (30,000)      |
| 5 CASH AFTER LOAN<br>ACTIVITY   | 11,648         | 4,215         | 8,281         | 3,598         | 18,015        |

## Managing a Cash Flow Defecit

A cash flow deficit arises when payments are due and the cash balance is too low to meet the obligations. In our example, the organization has a cash flow deficit of \$10,785 for the month of January. This doesn't necessarily mean that the organization is running an overall deficit. It simply means that at a specific point—in this case January—the organization does not have enough cash to pay its expenses.

Again, since your cash flow projection tells you when you will need additional cash, you are making time for your organization to explore its options. (That, of course, is the purpose of the cash flow projection: it gives you time to plan for deficits rather than reacting at the last minute.) When you do have a cash flow shortage, it's important to remember that there are some expenses you must pay on time. These include payroll, payroll taxes, and insurance.

How do you manage a cash flow shortage? There are several ways, but one of

the most common is to use a line of credit (line 4) from a local bank, as did the organization in our example. A line of credit helps smooth over fluctuations in cash flow. And, aside from closing costs when the line of credit is opened, there is no cost or interest assessment to your organization unless you actually use the line of credit. Because it may take a few weeks to several months to close a line of credit, you should apply for one well before you need it, preferably when you have a cash surplus.

In our example, the organization has a \$30,000 line of credit (line 4) with a bank. In January, it used \$15,000 of this line of credit to cover the cash flow deficit. The resulting cash after loan activity (line 5) is \$4,215, meaning that bills will be paid and there will be a slight cushion for the following month.

In addition to the line of credit, there are other ways to address a cash deficit:

**Obtain a short-term loan.** A number of nonprofit lenders and for-profit banks provide short-term loans to nonprofit organizations. These institutions provide "working capital loans" intended to help nonprofits cover operating expenses while they are waiting for a grant or contract disbursement. Generally, these loans are for a short term (less than 90 days) and you will be expected to repay them once the funds from the grant or contract are received.

**Speed up collection of accounts receivable.** Sometimes, you may be able to speed the collection of money that is owed to you. For example, if there are government agencies that owe you money, you could ask for an upfront payment in advance of the scheduled payment. Or, a foundation may be willing to rearrange its disbursement schedule if you anticipate a cash deficit. Again, the cash flow statement can help you structure your receivables with your funders to avoid cash flow deficits.

**Increase fundraising efforts.** Because your cash flow projections show when to expect cash flow surpluses and deficits, you might consider rearranging your fundraising schedule to accommodate your cash flow needs. For example, you could move a direct-mail appeal to an earlier date if you know you will need income sooner in the year.

**Liquidate investments.** Perhaps there are stocks, bonds or certificate-of-deposit accounts (CDs) that you can liquidate. If you are investing in CDs, you can structure them so that they mature when you need the cash. For example, the organization in the example could have opened a CD during the previous year that matures in the month of January, providing much needed

funds and limiting the organization's reliance on its line of credit.

**Cut expenses.** There may be expenses in your budget that could be deferred or cut. It's important that you keep an eye out for line items that continue to outpace your budget.

**Delay payment to vendors.** If you're really in a bind, you may want to consider negotiating with your vendors. Perhaps you have bills that are due within 30 days that can be extended to 60 or 90 days. Explaining your situation honestly and requesting a revised payment schedule is much better than simply ignoring the bills. Again, expenses that you should not ignore include payroll and payroll taxes. These should be your first priority.

## **Managing a Cash Flow Surplus**

A cash flow surplus occurs when your income exceeds your expenditures. Let's return to our previous example. The nonprofit has operating income (line 1) of \$44,417 in April, in addition to its beginning cash balance (line 2) from the previous month of \$3,598, for a cash surplus (line 3) of \$48,015. The nonprofit wisely chooses to pay off its \$30,000 line of credit (line 4), allowing enough in its account for the following month (cash after loan activity, line 5), a little over \$18,000.

Just as with a deficit situation, it is important that you anticipate and plan how you will manage your cash flow surplus. Options include:

**0** Use the idle cash to pay down your line of credit or outstanding loans. In our example, the organization paid down its line as soon as the funds were available—a wise choice, since paying off debt as soon as possible ultimately decreases the amount paid in interest.

**Invest in short-term instruments.** Through safe, low-risk investments, you can add interest income to your bottom line. The nonprofit in the example above may want to consider, depending on its cash flow projections for the next six months, a short-term investment.

**Invest in liquid instruments.** If your nonprofit carries a cash balance in its accounts from month to month, you may want to consider investing the cash surplus in a liquid account, such as a money market.

**Purchasing.** Use the surplus to buy supplies that you will use over the course of the year at a reduced, volume rate.

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