Cash Flow Forecasting

limelight

“If you cannot measure it, you cannot control it.”

-Lord Kelvin

Cash flow is the lifeblood of an organization - especially for startup and small organizations. It is critical that management can effectively forecast the current state of their cash, so they can meet their short and long-term operational needs.

Keep Up with the Demands of Ever-Changing Operations

The demands of your business are constantly evolving. Treasury groups are gravitating to more strategy-based roles in organizations (as opposed to functional roles) as management relies on their information for key decision making. Growing business have constant changes in their operating requirements and your business processes must remain streamlined, flexible and agile to stay current. That means your Cash Flow Forecasting solutions need to keep up as well.

Cash flow forecasting must look ahead to long term requirements, yet also consider what is required today. To this end, a cash flow forecasting solution must deliver:

- Real-time reporting that ensures your executives can make quick, informed decisions
- Integration with your existing systems and tools of choice
- Centralized data sources and data collection
- Pre-built workflows and templates
- Driver-based planning and forecasting with dedicated reports and templates
- Collaborative planning across your organization, down to individual branches and agents

Limelight helps you tackle these challenges and is the ideal cash flow forecasting solution for your organization. Speed up planning and reporting cycle times with an integrated cash flow forecasting solution.

Effective planning is critical when trying to keep up with cash obligations and changes in your daily operations. Long, manual reporting cycles can leave you well behind the competition - and the demands of your customers, whose loyalty you don’t want to test.

When you can see your cash obligations clearly and use model simulations for future cash flow forecasting, you can quickly adapt to your operational requirements and make sound business decisions. You can easily share and collaborate on these models and projections and ensure everyone in your organization is on the same page.

Limelight Cash Flow Forecasting Functionality

Limelight is a cloud-based cash flow forecasting solution can help you make sound and strategic business decisions by:

- Standardizing your cash flow reporting through integrating financial statement preparation
- Creating multiple scenarios in real time for daily operational objectives and long term strategic decision making
- Using dashboards/charts to show cash on hand, cash tied up in working capital, % cash requirements for capital projects, % invested, cash in multiple currencies, and any other key metrics displayed in real time

Purpose

Cash flow forecasting allows internal and external stakeholders to achieve their objectives in planning and allocating resources. Limelight's cash flow forecasting functionality allows you to make intelligent decisions based on the latest data, using predictive modeling techniques and manual overrides for management adjustments.

Objectives

Organizations must meet both short and long-term cash obligations. Analysis of your cash position and projections are often required on a daily, weekly or monthly basis depending on the financial position of the business. Accurate forecasting is essential to avoid potential pitfalls, reduce borrowing costs and invest excess cash in other strategic initiatives. Specific cash flow forecasting objectives include:

- Short-term liquidity management for operational needs
- Strategic capital investment planning for capital projects, acquisitions
- Short-term investment profits planning
- Long-term investment planning
- Dividend planning- for example subs to HoldCo and HoldCo to shareholders
- Optimal intercompany cash allocation and tax strategies
- Operational performance reporting
- Company credit ratings
- Share repurchase planning
- Debt covenant compliance
- FX exposure management

Limelight Cash Flow Forecasting Functionality

Pain Points

Most organization's current cash flow planning and forecasting processes are not precise enough to make sound business decisions. There are many variables and assumptions which can affect predictions, such as multiple inconsistent sources of input that are not readily available. In many cases the process is Excel-based, time-consuming and error-prone. Turnaround is long and there are many unknowns, which hamper your process. In surveys, 80% of clients indicate the following challenges encountered when it comes to cash forecasting:

- Lack of understanding of preparation processes
- Poor communication between functions (treasury, accounting, FP&A, management, etc.)
- Delayed visibility of cash flows
- Time-consuming to prepare, cash forecast is irrelevant by the time it is completed
- Risk of errors and omissions
- Reporting may not align with actual management of cash accounts by treasury

Considerations

The following must be considered before proceeding with a cash flow forecasting model:

- Cash forecasting culture – i.e. centralized or decentralized
- Collaboration and communications to key stakeholder and contributors
- Cross-functional ownership
- Indirect or direct cash flow methodology
- Optimal forecasting techniques
- Variables, parameters and assumptions
- Variance analysis – plan to actual
- Data gathering / data integration

Pitfalls to Avoid

- Applying automation to ineffective process
- Not tailoring the solution to target audience
- Employing a fragmented approach leading to inaccurate forecasts
- Overcomplicating unnecessarily (i.e. the 80/20 rule is not applied)
- Scripting assumptions and variables directly in the predictive model (in effect taking it away from end users)

The Limelight Solution

Limelight's cash flow forecasting solution approaches the problem from the balance sheet planning perspective. The process starts with forecasting the balance sheet with accurate and real-time data using historical trends, financial ratios and management adjustment layers. Users no longer need to manually work backwards from the balance sheet to prepare a cash flow statement. In Limelight the two statements are prepared in parallel, with the accuracy and data stakeholders need to get a complete view of the company's financial health.

Limelight's advanced features and functionality can yield the following benefits:

- Better management of cash obligations
- Maximized yields on investments
- Intelligent intercompany cash allocation decisions
- Streamlined planning for future investments
- Improved financial governance and compliance

Limelight Features and Benefits

Limelight Feature	Benefit
Reduced Risk	**Stress-test compliance scenarios** with advanced modeling to better predict outcomes and manage compliance risk before they become reality.
Repeatable Daily/ Weekly/ Monthly Refreshes of Data	**Real-Time Accurate Forecasting** Timely, accurate, reliable forecasts refreshed in real time as factors/ drivers/ historical actuals change. Scheduled and on-demand refreshes are available.
Qualitative & Quantitative Information	**High Quality, Useful Information** Statistical data such as growth rates, financial ratios, management adjustments can be used to calculate cash inflows/outflows. Creating a precise cash flow forecast based on real business transactions.
Integrated Financial Planning	**Consistent, Reliable Reconciliation of Subledger to General Ledger** Limelight provides the ability to create transactional level business models that directly feed a consolidated financial model to create a holistic view of the business and to help reconcile and drill into detail when required.
External Data Integration - Direct Access to Any External Database or Upload File	**Business Automation / Improved Efficiency** Source transactional data is imported into Limelight. Human error is significantly reduced, and provides a basis for planning. Reduce your planning and reporting cycle times (often by as much as 50%) thanks to Limelight's seamless database integration.
Data Integrity/ Single Source of Truth	**Single Source of truth** Detailed transactional models are configured based on the exact, unique needs of the function (i.e. employee payments, capital expenditures, project/job costs, collections, supplier payments, etc.). This information then flows to the consolidated financial model to understand the entire cash effect.

Limelight Features and Benefits

Limelight Feature	Benefit
Non-Finance Contributors	**Enhanced communication,** using a bottom-up method to predict cash flow gets input from those directly involved in the day-to-day running of the business. More accountability, more accuracy, directly going to the source. Keep your entire organization informed of the latest scenarios and outcomes and allow the right people to contribute at the right time.
Scenario Planning	**Be prepared for the future** with real-time scenario planning. Any slight adjustment in in the market or strategic outlook assumptions etc. will be accounted for immediately. Create a proactive culture.
Various Transactional Models	**Improved Team Integration and Business Monitoring** Any number of detailed Limelight planning models can be created and consolidated back into a financial model to improve business monitoring and understand the true impact of all relevant business transactions.
Multiple Calculation Methods by Type/Account	**Increased user adoption** with prebuilt calculations. Meet the exact needs of all business units and HQ with the ability to calculate any cash related transaction (billings, receivables, cash receipts, prepaid revenues, direct costs, payables, deferred costs).
Enhanced Visibility	Use models, **dashboards** and reports to maintain full visibility into your key metrics at all times.

Technical Overview of Balance Sheet & Cash Flow Forecasting Functionality

The following example illustrates some of the steps required for developing a balance sheet, which can then be used to feed into a cash flow forecast.

Assets

In this section, some items that are modeled during the planning process include cash, accounts receivable, and changes to fixed assets. Of course, this list is not exhaustive, and there may be a host of other items that are of interest (inventories, investments, etc.). Cash is impacted by many accounts in the model, but it also serves another function as well - that of a “calculated plug”. This value for cash can be either positive or negative (i.e. in the case of bank indebtedness) and serves as a balancing item on the balance sheet during forecasts. The two accounts that serve as cash plugs in Limelight model are (Cash) and (Bank Indebtedness). There is also an account that is used to track cash in the bank. The two cash plug accounts are not actual general ledger accounts, but they may represent a number of GL accounts.

Accounts Recievable

Accounts receivable (A/R) is frequently forecasted by analyzing the statistical measure Days Sales Outstanding (DSO). Days Sales Outstanding (DSO) is an activity ratio that indicates how many days, on average, it takes to collect a day’s sales revenue. DSO is calculated as:

DSO = (Accounts Receivable/(Revenue/365))

This ratio allows users to analyze the relationship between sales and the resulting accounts receivable levels that follow.

In Limelight, DSO can be used as a planning tool in addition to its use as a measurement of financial performance. During planning, users are able to enter the DSO for a specific period and have Limelight generate the correct Accounts Receivable amount for that DSO value. A formula can be used to create a relationship between DSO, sales, and A/R.

For example, if a company were to budget current year A/R account (say, GL1300) based on prior month's actual in a forecast version, one would want to be able to input the amount of days outstanding. A statistical account would be created to calculate the daily sales. If the account were to be called 'Daily Sales' [DS], the formula would be [GL1300]/30. A second statistical account would be created to input the number of days (for example account 'Days AR' [DSO]). The budget formula for [GL1300] would be DSO * Prior Period Daily Sales.

The DSO calculation can be used in many ways. For example, it may not be last months' data one wants to refer to but rather the same month one year ago. The combination of statistical accounts along with intelligent calculations will enable each company to formulate how their AR amount is derived.

Fixed Assets

The treatment of Fixed Assets in Limelight can be easily accomplished through the creation of a Fixed Asset Continuity schedule to track new additions. In conjunction with the Depreciation figures used in the P&L, calculations for Net Fixed Assets can be embedded into accounts using formulas. The general concept for a fixed asset schedule is that there will always be a running balance for many fixed asset items such as equipment, furniture and vehicles. If these items are tracked individually, they need to have their own corresponding accounts in the general ledger.

For planning purposes, these items may be tracked individually - or together as a lump sum amount under one fixed asset account. One recommendation is to setup several accounts for fixed assets and group them based on asset classes. In this scenario, you can have one fixed asset account for tracking changes to equipment, while another one could be used to track changes to company cars.

Through the use of the supporting schedules feature, users can enter their own capital additions under specific account categories while budgeting. For example, if there is an account category called "computer equipment", users can budget for their computer acquisitions by utilizing the supporting schedule and adding comments about planned purchases. This enables users to enter individual transactions and their associated costs, such as "bought 10 computers for new projects" in the equipment account for specific department.

Usage of fixed assets is captured through the depreciation schedule and would have its own accounts (one for depreciation expense and another for accumulated depreciation) in the model. As with fixed assets, there may be many depreciation accounts in the ledger corresponding to different asset classes. The premise of the continuity schedule is to begin with an account that will hold the balance for a fixed asset, then have another account that tracks the changes, and finally use a third account to accumulate the depreciation figures off the P&L.

A sample net fixed asset calculation is illustrated below:

Net Fixed Asset = Fixed Asset + Fixed Asset Additions – Accumulated Depreciation

We can understand this formula by examining the attributes for each account. The 'Fixed Asset' account can be for any class of asset such as equipment. When detailed analysis is required; each asset would have its own account and associated depreciation. For budgeting purposes, this account captures the changes in the balance of equipment during the year. Therefore, formula logic can be used to pick up the closing balance from the previous period and add changes due to additions/subtractions (i.e. the 'Fixed Asset Additions' account). Individual additions to fixed assets can be itemized through the use of the supporting detail schedules in data entry.

Through the use of Line Item Schedules, it is possible for users to enter additional details regarding fixed asset purchases without creating new accounts in the ledger. These line items are totaled back into the monthly totals for the account they are associated with. Each class of fixed assets can have an account tracking the additions, along with supporting line item schedules that list individual purchases.

Liabilities

The key components in the liabilities portion of the balance sheet are the different forms of long and short-term debt. Another important component liability is the accounts payable that may be due during the planning period. Accounts payable is an input for both actual AND budget versions. This leaves considerable room for adjusting A/P balances during the planning process. With respect to cash flow, A/P impacts the working capital portion of the statement.

Another common approach is to calculate A/P forecasted levels based on DPO (Days Payables Outstanding) historical trends - an approach similar to DSO for A/R described earlier. Limelight then derives A/P forecast based on the P&L planned COGS using the following formula:

DPO = (Accounts Payable/(COGS/365))

This ratio allows users to analyze the relationship between COGS and the resulting accounts payable levels that follow.

Equity

The equity portion of the balance sheet consists of retained earnings and paid-in capital (or capital stock). Setting up the retained earnings account - so that it picks up the net income amount – is a formula that adds the previous period's closing balance to the current period's net income. The paid-in capital amount can either be loaded for actuals or entered directly for the budget version. There is one item that is linked to paid-in capital, and that has to do with cash flow. Any change to paid-in capital is viewed as a financing activity on the cash flow statement. Therefore, an account needs to be created to capture changes in the cash flow component.

Foreign Currency Adjustment (Multi-Currency Models Only)

If a business operates in multiple currencies, another account needs to be created in the equity section. This account will act as a balancing account for differences in values during consolidation due to fluctuations in foreign exchange rates.

Balance Sheet Plug

The final step to constructing the balance sheet component in Limelight is to create a balance sheet plug. This plug contains the outstanding difference between total assets and total liabilities plus equity. It will force the balance sheet to balance by assuming a positive or negative cash balance. If the cash plug is negative, a situation of bank indebtedness occurs.

Method 1

The simplest way to force budgeted balance sheet to balance is to define a single account that automatically assumes the value of the difference between total assets and total liabilities and equity. While any account may be used, typically Cash is the account used to plug the balance sheet difference.

Method 2

In the first example, if total assets exceeded total liabilities and equity, then a negative value would appear in the Cash account. This however may not be very informative from a management-reporting standpoint. A slightly more complex calculation method involves using more than one account to force the balance sheet to balance. In this example, two accounts - ‘Cash’ and ‘Bank Indebtedness’ - are used. If total liabilities and equity exceeds total assets, the difference is placed in the Cash account, increasing assets as needed to force the balance sheet to balance. If total assets exceed total liabilities and equity, then the difference is placed in the Bank Indebtedness account, increasing total liabilities and equity and again creating the required balance.

Summary

Developing a balance sheet and cash flow component to supplement an already existing P&L structure in a Limelight model is not difficult. The examples described above merely illustrate one possible approach to developing this model. There are countless ways to create the balance sheet and cash flow components. However, the concepts discussed are still the same regardless of the methodology.

The balance sheet and cash flow components should be developed with maximum flexibility to enable adjusting as necessary during the planning cycle. Limelight’s features and functionality provide a robust platform – in conjunction with the general ledger and other supporting schedules - to build a functional balance sheet and cash flow planning system.

Overview of Limelight

As a cloud-based solution, Limelight is easy to deploy across your organization. It integrates with your data sources and uses the Microsoft Excel features you and your team know and love. With its intuitive user interface and its ability to manage large, complex databases, you'll realize faster plan runtimes almost immediately.

With Limelight, you can model claims and sales commissions, track and analyze variances in real-time, forecast renewals and new business, plan departmental expenses and salaries. With Limelight's workforce planning features, you can even track and manage your staffing requirements.

Our professional services team closely with all of our Limelight clients to ensure your implementation runs smoothly and efficiently, and we offer training—in person or online—to ensure your team is ready to run with Limelight in no time.

Key features of planning and budgeting with Limelight include:

Planning and Budgeting

- Conduct expense and headcount planning to proactively identify cash flow and talent gaps
- Manage financial planning, operational budgeting and sales planning from one central location
- Specify costs, rates and currency globally, or on a project or resource basis

Variance Analysis

- Plan for long-term success by tracking actual and planned outcomes in real-time
- Adjust on the fly as costs, budgets and regulations change
- Track variance on both the macro and micro level as needed

Premium Modelling

- Model revenue using multiple dimensions and drivers, including commissions and loss ratios
- Model your cash flow, profit and loss underwriting and balance sheets
- Model profits against new and returning business revenue

Overview of Limelight

Expense Planning

- Easily track expenses with detailed reporting dashboards
- Analyze costs and their impact on claims and assessments
- Plan for future costs based on past results

Headcount Planning

- Transfer employees from one cost center to another
- Use smart lists to manage and adjust headcount
- Plan compensation, bonuses and other benefits

Sales Compensation Planning

- Forecast your producers' salaries and commissions
- Build compensation plans that motivate and reward your top performers
- Review and report on results from producers, account managers and regions

Communication and Collaboration

- Share key information with some or all branches and agents
- Create specific groups and teams to collaborate together
- Set access levels using enterprise-grade security features

Project Reporting

- Report on P&L by product and/or lines of business
- Compare targets, forecasts, and real vs. actual results
- Access profitability reports to see which lines of business are generating the most revenue

Contact Us

Learn More About Limelight

hello@golimelight.com

1 (877) 931-9292

4950 Yonge Street, Suite 2308
Toronto, Ontario M2N 6K1