Enterprise Budgets, Forecasts and Cashflow for Enterprise Success

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Presenter

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Course Outline

Learning Outcomes

- Understand the importance of budgeting, forecasting and cash flow analysis
- Understand how to prepare a meaningful and effective budget
- Understand how to perform a forecast that supports enterprise success
- Understand how to perform a cash flow analysis that supports enterprise success; and
- Understand the advisory role of the accountant

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Quote

Almost every business in South Africa is faced with an uncertain future. To maximise the chances of survival, every company and board will need to conduct an honest assessment of the business and market environment, understand the available support, engage with its stakeholders and implement the changes that are required to maximise the chances of its survival. This process will need to be redone many times over the coming years and many companies will no doubt need to downsize or change their business model to survive. Those that act quickly and decisively are going to be best placed to not only survive, but thrive in the aftermath of the COVID-19 pandemic.

- John Evans CA(SA) via Accountancy SA

MODULE 1

THE IMPORTANCE OF CASHFLOW MANAGEMENT IN A COVID-ECONOMY

The Importance of Cashflow Management in a COVID-Economy

- In an unpredictable economic environment, taking a comprehensive view of cash flow and setting priorities for spending is vital.

- COVID-19 has taught us that a single event can trigger a cascade of risks affecting all aspects of an entity’s operations.

- The pandemic, combined with global trade tensions, ongoing political elections, continued social unrest in some countries, and other risk drivers, has put tremendous strain on most organisations.

The Importance of Cashflow Management in a COVID-Economy

- Revenues that were once fairly predictable are no longer stable or even present, and organisations trying to navigate the crisis face previously unseen costs.

- COVID-19 and other 2020 events have affected almost all aspects of most organisations, making it challenging to pinpoint all potential variables that might affect cash inflows and outflows simultaneously.

- In this environment, finance leaders should consider taking a number of steps to obtain a better, more comprehensive view of organisational cash flows.

The Importance of Cashflow Management in a COVID-Economy

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The Importance of Cashflow Management in a COVID-Economy

- **Start with cash inflows**
  - What are the core sources of cash for our organisation?
  - How is the current business environment (the pandemic, ongoing national elections, social unrest, etc.) affecting each of these core sources of cash?

The Importance of Cashflow Management in a COVID-Economy

- **Dissect cash outflows**
  - What are the most significant types of cash outflows for our organisation?
  - What expenditures can be categorised as fixed or variable?
  - How is the current business environment affecting cash outflows?
  - What amount of discretion is available to manage cash outflows?

The Importance of Cashflow Management in a COVID-Economy

- **Develop multiple scenarios**
  - Worst case
  - OK-but-not-great case
  - Reasonable, hopeful best case

The Importance of Cashflow Management in a COVID-Economy

- **Develop multiple scenarios**
  - Worst case
  - OK-but-not-great case
  - Reasonable, hopeful best case

The Importance of Cashflow Management in a COVID-Economy

- **Take advantage of scenario-planning and forecasting tools**
  - Excel/ What if
  - Oracle Crystal Ball add-on software for Excel
  - Monte Carlo Simulation
  - Xero
  - FutrLi
  - Spotlight
  - Fathom

The Importance of Cashflow Management in a COVID-Economy

- **Rank possible cash flow solutions**
  - Identify expenditures that can be delayed or halted
  - Renegotiate supplier/vendor terms
  - Leverage benefits of financial markets
  - Identify assets or operations that might be sold
  - Evaluate payroll options
  - Consider government funding options

Module 2

Budgeting Basics

Budgeting Basics

A budget is an outline of expectations for what a company wants to achieve for a particular period, usually one year. Characteristics of budgeting include:

- Estimates of revenues and expenses.
- Expected cash flows.
- Expected debt reduction.
- A budget is compared to actual results to calculate the variances between the two figures.

Budgeting Basics

- Budgeting represents a company's financial position, cash flow, and goals.

- A company's budget is usually re-evaluated periodically, usually once per fiscal year, depending on how management wants to update the information.

- Budgeting creates a baseline to compare actual results to determine how the results vary from the expected performance.

Budgeting Basics

- While most budgets are created for an entire year, that is not a hard-and-fast rule.

- For some companies, management may need to be flexible and allow the budget to be adjusted throughout the year as business conditions change.

MODULE 3

FINANCIAL FORECASTING BASICS

Financial Forecasting Basics

- Financial forecasting estimates a company's future financial outcomes by examining historical data.

- Financial forecasting allows management teams to anticipate results based on previous financial data.

Financial Forecasting Basics

Characteristics of financial forecasting include:

- Used to determine how companies should allocate their budgets for a future period. Unlike budgeting, financial forecasting does not analyze the variance between financial forecasts and actual performance.

- Regularly updated, perhaps monthly or quarterly, when there is a change in operations, inventory, and business plan.

Financial Forecasting Basics

Characteristics of financial forecasting include:

- Can be created for both short-term and long-term. For example, a company might have quarterly forecasts for revenue. If a customer is lost to the competition, revenue forecasts might need to be updated.

- A management team can use financial forecasting and take immediate action based on the forecasted data.

Financial Forecasting Basics

- Financial forecasting can help a management team make adjustments to production and inventory levels.

- Additionally, a long-term forecast might help a company's management team develop its business plan.

MODULE 4

BUDGETING VS FORECASTING

Budgeting vs Forecasting

Budgeting and financial forecasting are tools that companies use to establish a plan for where management wants to take the company—**budgeting**—and whether it is heading in the right direction—**financial forecasting**.

Budgeting vs Forecasting

Although budgeting and financial forecasting are often used together, distinct differences exist between the two concepts.

- Budgeting quantifies the expectation of revenues that a business wants to achieve for a future period, whereas

- financial forecasting estimates the amount of revenue or income that will be achieved in a future period.

Budgeting vs Forecasting

- Budgeting is the financial direction of where management wants to take the company, helping quantify the expectation of revenues that a business wants to achieve for a future period
- Financial forecasting tells whether the company is headed in the right direction, estimating the amount of revenue and income that will be achieved in the future.
- Budgeting creates a baseline to compare actual results to determine how the results vary from the expected performance.
- Financial forecasting is used to determine how companies should allocate their budgets for a future period, but unlike budgeting, financial forecasting does not analyze the variance between financial forecasts and actual performance.

Budgeting vs Forecasting

- A budget is an outline of the direction management wants to take the company. A financial forecast is a report illustrating whether the company is reaching its budget goals and where the company is heading in the future.

- Budgeting can sometimes contain goals that may not be attainable due to changing market conditions. If a company uses budgeting to make decisions, the budget should be flexible and updated more frequently than one fiscal year so there is a relationship to the prevailing market.

- Budgeting and financial forecasting should work in tandem with each other. For example, both short-term and long-term financial forecasts could be used to help create and update a company's budget.

MODULE 5

PREPARING A MEANINGFUL AND EFFECTIVE BUDGET

Preparing a meaningful and effective budget

Back to Zero based budgeting

1. Evaluate current business model/ strategy
2. Strategise and decide on future business model/ strategy
3. Identify your revenue streams
4. Identify the drivers for each revenue stream (equation)
5. Estimate revenue per revenue stream
6. Estimate the costs necessary to generate the estimated revenue streams

   (KEY POINT = Every cost needs to contribute towards generating revenue)

Preparing a meaningful and effective budget

Back to Zero based budgeting (continued)

7. Include savings (at least 3-6 months operating cashflow in the bank at all times)
8. Be super realistic about revenue streams
9. Relook at fixed costs - can they be turned into variable costs?
10. Relook at costs that don’t strongly correlate with revenue generation - are they really necessary?
11. Write down the steps necessary to move from current situation to budgeted situation

Preparing a meaningful and effective budget

Back to Zero based budgeting (continued)

12. Be agressive with identifying and executing strategies for additional revenue generation (think complimentary products/ services, affiliate marketing, additional monetisation strategies)
13. Use resources more than once in generating revenue
14. Save costs through collaborations and working with others in your industry
15. Be aggressive & intentional about creating passive income streams

Preparing a meaningful and effective budget

BLOG	+	Youtube	+	Social Media	=	Adsense$ + Affiliate$ + Ticket$ + Book$ + Course$ + Shop$							Longterm
Write Courses	+	Record Courses			=	Course$							Longterm
Conversations with New Potential Tribe Members	+	Happy Current Tribe Members			=	Membership$							Short term + Longterm
Linkedin Conversati	+	Networking Affiliates	+	Happy Customer Referrals	+	Invites to Linkedin Event	+	High Converting Landing Page	+	Increased website Traffic	=	Ticket$	Short term + Longterm
Write 1,500 Words	+	Proofread 1,500 Words			=	ListVerse$							
Recruit Affiliates	+	Manage Affiliates	+	Product Uploads	=	Shop$	***Educate members on how to recruit affiliates and why it is important***						
Record Webinars					=	SAAA$							
Write Book	+	Publish Book			=	Book$							
Tzippy	+	Accounting Referrals			=	Accounting$							

Module 6

Financial Forecasting

Financial Forecasting

- COVID-19 is fundamentally reshaping how businesses and finance teams forecast.
- Cash reserves are more vital than they’ve ever been.
- Revenue fluctuates wildly as customers abandon or reduce contracts.
- Businesses are incurring new expenses that simply didn’t exist a couple of years ago.

Financial Forecasting

- Budgets tighten as margins grow thinner.
- By the time a finance team delivers the latest round of forecasts and budgets to the C-suite, they’re outdated and it’s back to the spreadsheets.
- This means adopting a rolling financial plan that accounts for transaction-level granularity.

Financial Forecasting

- According to a recent Accenture survey of CFOs and finance leaders, 99% of respondents believe that operating with real-time data is critical to navigating disruptions like a global pandemic, economic downturn, or natural disaster.

- Sixty-eight percent reported that real-time financial modeling will be critical to better business decision making, more accurate forecasting models, and improved data accuracy.

Financial Forecasting

- The systems and technologies in place should also allow finance teams to pull this data swiftly and more frequently without the need to update line items in a spreadsheet.

- Real-time reporting could mean finance teams are providing financial updates on a weekly or biweekly basis instead of monthly or quarterly.

- More importantly, they have the ability to provide the C-suite with a range of models the second a crisis hits so business leaders can make more informed decisions about workforce planning, spending, and more.

Financial Forecasting

- Every business is dealing with a high degree of volatility, uncertainty, complexity, and ambiguity that ultimately affects forecasting demand.

- B2C businesses are subject to changes in consumer behavior as, say, unemployment rates increase or overall consumer spending plummets.

- B2B companies are at the mercy of their own customers’ overall business health.

Financial Forecasting

- Forecasting the consequences of market fluctuations has to be more comprehensive and embedded in day-to-day operations.
  - What happens to cash flow and revenue if 20% (or 35% or 60%) of customers reduce or cancel contracts?
  - How do those customer decisions influence marketing spend or recruitment efforts?

Financial Forecasting

- Financial forecasts are often structured using categories of products or services the business sells, and they don’t always include the required depth of information about customers.

- Having up-to-date information about customer segments and about individual customer health is vital to building a reliable forecast.

Financial Forecasting

- Start feeding real-time customer data into the forecasting model.
  - What kind of behavior are you seeing from customers?
  - Are they making new demands or changing their requirements? I
  - n a retail business, you could monitor which customers are most at risk of churn, assessed by the number of support tickets they have raised and how quickly they're resolved. What would be the impact of losing these particular customers?

Understanding these customer behaviors is much more likely to lead to accurate predictions.

Financial Forecasting

- This approach may also form the impetus for a more strategic approach to resource allocation.
  - Can you invest in more support staff to increase their satisfaction levels and prevent customers from dropping contracts?
  - Are you seeing customer demand decrease for any particular service?
  - How does that impact staff composition and overall organizational health?

Looking at the forecast through a customer- or sales-centric lens can help to highlight trends and new propositions or products in which businesses should invest now or in the future.

Financial Forecasting

FIGURE 3: STATIC BUDGETING VS. DYNAMIC STRATEGIC PLANNING

STATIC BUDGETING	DYNAMIC FORECASTING AND PLANNING
Overreliance on historical data and precedence to make decisions	Flexible and agile goals that can adapt to market conditions
Data is siloed between departments	Democratized data across the organization
Targets and goals are fixed	Real-time flow of data enables dynamic decision making

Module 7

Cashflow Analysis - things to consider

Cashflow Analysis - things to consider

Ensure you have a robust framework for managing supply chain risk.

- Supply chain management is a complex challenge, and finance-related problems only add to the risk.

- Do you know if any of your customers are in trouble and might be unable to pay for the goods and services you deliver?

Cashflow Analysis - things to consider

Ensure you have a robust framework for managing supply chain risk.

- If you manufacture a product and want to sell it to someone outside your borders, you typically require a letter of credit from a prime bank that proves the buyer can pay.

- This letter of credit not only provides a source of ultimate payment, it can also be used to secure inventory financing while the goods are in transit—so it's important to make sure these letters of credit are still reliable.

Cashflow Analysis - things to consider

Ensure you have a robust framework for managing supply chain risk.

- Ensuring you understand the financial risks of your key trading partners, customers, and suppliers is a critical consideration in times like these.

Cashflow Analysis - things to consider

Ensure your own financing remains viable.

- In these circumstances, don't assume the financing options you previously had available to you will continue to be available.
- Undertake scenario planning to better understand how much cash you'll need and for how long.
- Use this opportunity to actively engage with your financing partners to ensure your available lines of credit remain available, and to explore new or additional options should you require them.

Cashflow Analysis - things to consider

Focus on the cash-to-cash conversion cycle.

- Under normal business conditions, companies primarily focus on the profit and losses–growing the top line while managing the bottom line.
- Routine back-office activities such as paying bills and turning receivables into cash are often taken for granted.
- In the current abnormal business conditions, smart companies are shifting their focus from the income statement to the balance sheet.

Cashflow Analysis - things to consider

Focus on the cash-to-cash conversion cycle.

- Of the three elements of supply chain working capital–payables, receivables, and inventory–, supply chain executives have a tendency to focus on inventory.

- But, in order to minimize working capital requirements during challenging times, it’s important to apply a coordinated approach that addresses all three areas.

Cashflow Analysis - things to consider

Think like a CFO, across the organization.

- As supply chain managers step up to the challenges of disruption and inventory shortages, they generally spend their days thinking about operations and don’t pay much attention to finance and treasury issues.

- More often than not, inventory levels and other critical business parameters are driven by customer service requirements and operational capabilities, not financial constraints.

Cashflow Analysis - things to consider

Think like a CFO, across the organization.

- But what if the situation was reversed?
- What if working capital was the company’s primary constraint on inventory, and supply chain managers were given the challenge of making it work?
- How would that affect your supply chain and inventory practices?

Cashflow Analysis - things to consider

Revisit your variable costs.

- Reducing your variable costs is often a quicker way to immediately reduce your cash outflows than focusing on your fixed costs.
- Of course, there are the typical variable cost-reduction levers, such as imposing travel bans and non-essential meeting restrictions (which might already be in place as a way to manage employee safety), imposing hiring freezes, and placing restrictions on discretionary spend like entertainment and training.

Cashflow Analysis - things to consider

Revisit your variable costs.

- When labour is a significant cost line in your business, consider avenues that might help reduce spend to avoid getting to a situation where layoffs are required.

Cashflow Analysis - things to consider

Revisit your variable costs.

- For example, look for opportunities to reduce contract labour and re-distribute work to your permanent workforce.

- Encourage employees to take available leave balances to reduce liabilities on the balance sheet.

- And, if necessary, consider offering voluntary, or even involuntary, leave without pay to preserve cash.

Cashflow Analysis - things to consider

Revisit capital investment plans.

- With cash flow forecasts in mind, consider what's really necessary for the near term.
- What capital investments can be postponed until the situation improves?
- What capital investments should be reconsidered?
- What capital investments are required to position for the rebound and for creating competitive advantage?

Cashflow Analysis - things to consider

Focus on inventory management.

- Companies are at risk of experiencing supply chain disruptions due to shortages in raw material and component parts.
- Inventory safety stock parameters will most likely need to be updated to reflect the increased demand and supply-side volatility, which will have the effect of increasing overall inventory levels, assuming that’s possible.

Cashflow Analysis - things to consider

Focus on inventory management.

- At the same time, businesses will be thinking about securing additional inventory, or strategic stock, as a further buffer against the potential impact of a prolonged or much broader supply chain disruption.

- Also at the same time, from a cash flow perspective, companies may be considering actions to reduce finished goods inventories, especially in perishable products, where waste is an important consideration and markets remain difficult to access.

Cashflow Analysis - things to consider

Focus on inventory management.

- Balancing the demands for more buffer inventory and managing cash flow may not be as easy as it sounds.

- Companies that still use simplistic approaches to inventory management might be able to do a quick assessment and find some immediate opportunities to drive down inventory.

- However, many companies are likely to find that significant inventory cuts have an adverse effect on customer service and production.

Cashflow Analysis - things to consider

Focus on inventory management.

- Sustainable savings will most likely require fundamental improvements in end-to-end supply chain inventory visibility, demand planning, inventory and safety stock policies, production planning and scheduling, lead-time compression, network-wide available-to-promise, and SKU (stock keeping unit) rationalization.

Cashflow Analysis - things to consider

Extend payables, intelligently.

- One way to preserve working capital is to take longer to pay your suppliers.

- Some companies may unilaterally decide to delay their payments and force the extension on their suppliers, especially when stuck with inventory they can’t deliver into impacted margins.

Cashflow Analysis - things to consider

Extend payables, intelligently.

- Of course, such an approach is likely to damage your supply relationships.

- Even worse, it might deprive supply chain partners of the cash they need to maintain their operations, which could lead to late deliveries and quality problems, never mind the added strain to supply relationships.

Cashflow Analysis - things to consider

Extend payables, intelligently.

- We recommend working with suppliers to establish an agreement that both of you can live with.
- There might even be situations where you need to accelerate payables for a critical supplier that is on the brink of failure in order to preserve the integrity of your supply chain and prevent a critical disruption.

Cashflow Analysis - things to consider

- **Manage and expedite receivables.**
- Companies tend to get lax about receivables when the economy is booming, interest rates are relatively low, and cash flow is not a concern.
- But, as supply chains are affected and managing cash flow becomes more important, it’s worth taking a hard look at how your receivables are being managed.

Cashflow Analysis - things to consider

- **Manage and expedite receivables.**

- In the point above, we mention the strategy of delaying payments to your suppliers; don’t be surprised if your customers are thinking about doing the same thing to you.

- That’s why it’s important to improve the rigour of your collection processes.

Cashflow Analysis - things to consider

- **Manage and expedite receivables.**

- Focus on customer-specific payment performance and identify companies that may be changing their payment practices.

- Also, get the basics right, such as timely and accurate invoicing.

- Any errors in your billing process can lead to costly delays in receiving payment.

Cashflow Analysis - things to consider

Consider alternate supply chain financing options.

- Depending on what your cash flow scenario planning reveals, you may also need to consider tactics to generate faster cash flow from your receivables.

- Aggressive techniques such as factoring your receivables, although relatively expensive, may be your best option to improve cash flow quickly.

Cashflow Analysis - things to consider

Consider alternate supply chain financing options.

- You may also consider working with your customers to offer dynamic discounting solutions for those that are able to pay more quickly (e.g., discount terms can be defined in advance, and the customer calculates the appropriate discount based on a defined payment schedule).

Cashflow Analysis - things to consider

Consider alternate supply chain financing options.

- With this technique, you are essentially paying customers to provide you with short-term financing.
- But the cost may be substantial:
- a conventional “2% net 10” early payment discount translates into a 36% APR (Annual percentage rate)
- However, if government loans or bank credits are not available, this might be one of your only options.

Cashflow Analysis - things to consider

Consider alternate supply chain financing options.

- There are also a number of other supply chain financing possibilities that can be implemented in the short to medium term, such as collaborating with your key trading partners to optimize cash flow across the extended supply chain.

Cashflow Analysis - things to consider

- **Audit payables and receivables transactions.**

- Make sure you’re paying the right amount for the goods and services you procure and collecting the right amount for goods and services you sell.

- On the payables side, double-check that you’re not overpaying duties and taxes on purchases, especially as alternate international supply locations are used to keep supply chains running.

- Also, if you have the cash flow to support it, make sure you’re taking full advantage of all available discounts.

Cashflow Analysis - things to consider

- **Audit payables and receivables transactions.**
- On the receivables side, look for situations where unearned discounts were applied and then aggressively pursue the proper payment.
- Once the audits have been completed, look for longer-term policy and process improvements that can prevent new problems from cropping up. Consider using robotic process automation for your audits, which will reduce the burden on headcount.

Cashflow Analysis - things to consider

Consider alternate or non-traditional revenue streams.

- If your scenario planning is showing pressure on your continued revenue streams, consider ways you could temporarily or maybe even permanently replace that revenue.

- For example, if your primary markets are international, how might you pivot to domestic markets (especially if your inventory is perishable)?

Cashflow Analysis - things to consider

Consider alternate or non-traditional revenue streams.

- If you have assets you use to generate revenue, how could you think differently about how those assets are used to generate alternate revenue sources?

- Not only could this reduce some of your top line pressures, it could also mean not having to reduce your cost lines as significantly (not to mention a potentially more diversified revenue mix in the longer term).

Cashflow Analysis - things to consider

Convert fixed to variable costs, where possible.

- In times of uncertainty, it's generally a good idea to swap fixed costs for variable costs wherever you can–preserving your core business while increasing your flexibility on the fringes.

- Selling assets and then leasing them back is one way to raise emergency cash.

Cashflow Analysis - things to consider

Convert fixed to variable costs, where possible.

- You might also want to consider expanding your use of practices such as contract manufacturing, transportation fleet leasing, and thirdparty warehousing.

- This is not likely a quick-hit measure for most companies, but may be important to longer-term cash flow management, depending on how long demand and supply chains are disrupted by COVID-19.

Cashflow Analysis - things to consider

Think beyond your four walls.

- To maximize working capital, you can’t only focus on your own operations and inventory levels: you need to think about your entire ecosystem and supply chain.
- Squeezing inventory out of your operation may not do much good– and could in fact introduce significant risk–if it just shifts the burden to a supplier or customer.
- The same is true for payables and receivables. It’s important to carefully consider the upstream and downstream impact of your actions.

Cashflow Analysis - things to consider

Think beyond your four walls.

- High-level financial risk assessments should be conducted on any critical, sole-source suppliers to identify issues before they become problems.

- In extreme cases, if a critical supplier is at risk, you might even need to buy a stake in the company or acquire the business outright to protect your supply chain and keep your goods and services flowing.

Appendix 1

Links

Links

[How business forecasting software will help you win clients over]

[Managing your cashflow - take control with Xero (Video)]

[Memo to the CFO: A new approach to 2021 budgeting starts now]

[How to save a company from the impact of COVID-19]

[Cashflow management in an uncertain world]

Questions

Thank you
for your participation