Cash forecasting best practices for midsize businesses

Use your cash position to move your business forward.

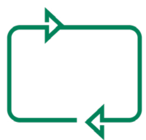
J.P.Morgan | CHASE

Mission-critical: cash forecasting

Cash forecasting is the process of estimating the amount of cash inflows and outflows your business expects to have over a specific period, usually a few months to a year. It helps you anticipate how much cash your business will have on hand at any given time, allowing you to make informed decisions about spending, saving and investing.

While most midsize business owners understand the importance of cash forecasting, many don't recognize how critical it is to positioning a company for reliable, sustainable growth. Owners often don't treat cash forecasting—or rather accurate cash forecasting—as mission-critical.

Accurate cash forecasting influences multiple critical areas of business, including:



Liquidity management

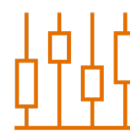
Cash forecasting helps you understand when your business is likely to have surpluses or shortages of cash. This allows you to manage your liquidity more effectively, ensuring you have enough cash on hand to meet your short-term obligations.

Financial planning

By forecasting your cash flow, you can better plan for major expenses, investments or growth opportunities. This helps you make informed decisions about how to allocate your financial resources.

Risk management

Cash forecasting can help you identify potential cash flow problems in advance, allowing you to take proactive measures to mitigate these risks. For example, you may decide to delay certain expenses or secure a line of credit to cover any shortfalls.



Strategic planning

Understanding your future cash flow can also help you make more strategic decisions about your business. For example, you may decide to accelerate certain projects or investments if you anticipate a surplus of cash in the future.

Credibility with stakeholders

Lenders, investors and other stakeholders often require businesses to provide cash flow forecasts as part of their financial reporting. Having accurate and reliable forecasts can enhance your credibility with these stakeholders.

Mission-critical: cash forecasting

When following best practices, cash forecasting isn't just about being able to pay your bills at the end of each month and having a positive bottom line. It enables you to plan for the future with a clear view of what you can invest in—be it equipment, technology or talent—and it better positions you to capitalize on growth opportunities. Cash forecasting is as essential to daily financial operations as it is to long-term decision-making.

In this guidebook, we'll explore the challenges midsize businesses face when it comes to implementing best practices in cash forecasting, the risks avoided by improving cash forecasting and the practical steps businesses can take to start cash forecasting like a financial savant. Business owners, executives and finance and tech teams all have a stake in better cash forecasting. Whatever role you play within the organization, this guide will provide valuable insight on improving business planning in the short and long term.

As always, we're here with ideas and solutions to help you run your business more efficiently. **Find out more or connect with a banker.**

The road to better cash flow

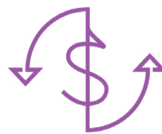
Cash flow and cash forecasting go hand-in-hand. They both require strong cash positioning. You can't develop a cash forecast without a clear understanding of your cash flow and cash position. And you can significantly improve your cash flow with an accurate cash forecast.

To perform cash forecasting, you typically start by analyzing your historical cash flows and identifying patterns and trends. You then consider factors that could impact your cash flows in the future: seasonal fluctuations, economic conditions and changes to your business operations. Finally, you use this information to create a cash flow forecast, which is a projection of your future cash inflows and outflows. An accurate cash forecast can improve day-to-day cash flow management by helping you better anticipate cash needs. By forecasting future cash flows, businesses can anticipate periods of high or low cash availability. This allows them to plan ahead and take actions to ensure they have enough cash on hand to cover expenses during lean periods.

Cash positioning vs. cash flow vs. cash forecasting

Cash positioning

Cash positioning measures how much cash you have at a single point in time. It's the process of aggregating all cash and liquid financial asset balances to provide a complete picture of a company's current state of liquidity. It helps to identify whether or not there is enough cash in each account to cover upcoming expenses while ensuring no account has excess cash. **Learn more about cash positioning.**



Cash flow

Cash flow is a historical record of where your cash went over a period of time. It looks at the movement of funds into and out of a business over a specific period, typically a month, quarter or year. It includes all cash flows from sales, investments and financing activities, as well as all cash outflows for expenses, purchases and debt payments.

Cash forecasting

Cash forecasting is a forward-looking process to calculate your positioning at a point in the future. Companies study their current positioning, their cash flow history and any expected changes in the business environment—such as sales growth, new investments or changes in market conditions—to predict what's ahead. Cash forecasting is used to anticipate cash shortages or surpluses and make informed decisions about how to manage cash flow in the future.

The road to better cash flow

What spoils await on the cash forecasting road to better cash flow?

> *"Regardless of company size, the most successful organizations make cash flow forecasting a core competency. It's a muscle that needs exercise. Businesses that don't forecast well find themselves in a reactive posture, scrambling to respond to setbacks rather than focusing on long-term value creation."*

Meredith Anderson
Vice President, Corporate Treasury Consulting

The risks you face when cash forecasting isn’t a priority

Inaccurate cash forecasting can lead to a range of financial, operational and reputational risks for businesses, including:

Cash shortages: Without accurate forecasting, businesses may not have enough cash on hand to cover their expenses, leading to cash shortages. This can result in missed payments to suppliers, employees or lenders, and that can damage relationships and potentially lead to financial distress.

Ineffective collection processes: Forecasting helps you keep tabs on your accounts receivable and can lead to more effective, better organized collections processes.

Overborrowing: Inaccurate forecasting can lead to overestimating cash needs, leading businesses to borrow more than necessary. This can result in unnecessary interest payments and increased financial risk.

Poor investment decisions: Without a clear understanding of future cash flows, businesses may invest in projects or initiatives that are not financially viable, leading to wasted resources and potential losses.

Lack of strategic planning: Inaccurate forecasting can hinder strategic planning efforts. Every business has a budget season, and not knowing a future cash position can drastically impact the amount of money companies allocate to various departments. This can result in missed opportunities for growth or failure to anticipate and mitigate potential financial risks.

Damage to reputation: Cash flow problems resulting from inaccurate forecasting can damage a business’s reputation with suppliers, customers and investors. This can make it harder to secure credit or attract investment in the future.

Legal and compliance issues: Failure to accurately forecast cash flow can lead to legal and compliance issues. For example, businesses may be unable to meet their tax obligations or may violate contractual agreements due to cash flow problems.

Implementing cash forecasting best practices

Now that we unpacked what cash forecasting is, how to do it and why it's important, let's talk about the best practices for developing a cash forecast.

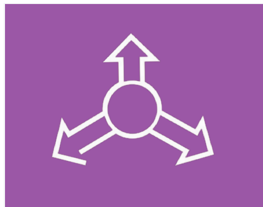
Determine your ideal approach—but be ready to adjust: There are various methods you can employ to develop a cash forecast depending on your size, industry and complexity. Rolling forecasts are recommended—instead of static forecasts that only updates monthly or quarterly—because they enable you to continually update your cash flow projections based on the latest information. This method can be combined with other foundational forecasting approaches, including:

Budget-based

Use budgeted income statements and balance sheets to estimate future cash flows. Project sales, expenses and capital expenditures to predict how these activities will impact your cash position.

Driver-based

Identify and monitor key drivers that impact cash flows, such as sales volume, pricing changes or payment terms.



Scenario analysis

Create multiple cash flow scenarios based on different assumptions and factors, such as changes in market conditions, customer behavior or economic trends to prepare for various outcomes that could impact your cash position.

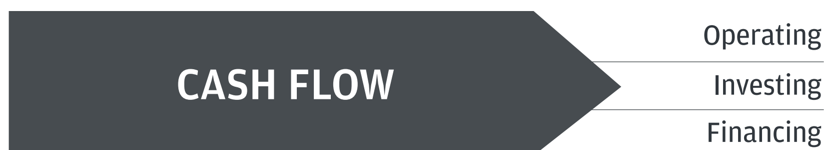
Cash flow modeling

Use mathematical models and algorithms to predict future cash flows based on historical data and assumptions. These models can range from spreadsheets to financial software.

Implementing cash forecasting best practices

Once you've determined your ideal approach, it's time to start applying the ideal tactics.

Segment cash flows: Break down cash flows into categories such as operating, investing and financing activities. This can provide a clearer picture of where cash is coming from and going to, helping to identify potential issues or opportunities.



Consider multiple scenarios: Develop and analyze multiple scenarios (e.g., best case, worst case and most likely) to understand the range of possible outcomes and their implications for cash flow.

Regularly monitor actual vs. forecast: The work of cash forecasting is never done. Compare actual cash flows to forecasted cash flows regularly to identify any variances and adjust forecasts accordingly. Cash flow forecasts should be reviewed and updated regularly to reflect changes in the business environment and ensure forecasts remain relevant.

Document your assumptions: Clearly document the assumptions underlying your forecasts, including factors such as sales growth, payment terms and economic conditions. This can help explain variances and improve the accuracy of future forecasts. You should also consider seasonality and cyclical trends that may impact cash flows, such as increased sales during the holidays or slower periods during other times of year.

Let tech do the heavy lifting: Cash forecasting software can automate the cash forecasting process, making it faster and more accurate. These tools can integrate with accounting systems to pull in relevant data and generate forecasts based on historical trends and future projections.

By following these best practices, midsize businesses can improve the accuracy and effectiveness of their cash forecasting process, leading to better cash flow management and more informed decision-making.

How JPMorgan Chase experts can help

The role of a JPMorgan Chase banker continues to evolve with the needs of our clients' businesses. From helping to improve day-to-day cash flow to long-term business planning, a banker dedicated to serving midsize businesses can provide you with information and assistance for many of the challenges you face. With access to the firm's full suite of experts and services, our bankers can connect you with the resources you need at every stage of your business journey. Whether optimizing for today or planning for the future, our bankers can help.

Visit **https://jpmorgan.com/middle-market-banking** to learn more, or **contact a banker** today.

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