2.5 Cash flow statements

Name: _____ Class: _____ Date: _____ **Total: 22 marks**

KEY WORDS cash flow statement • operating

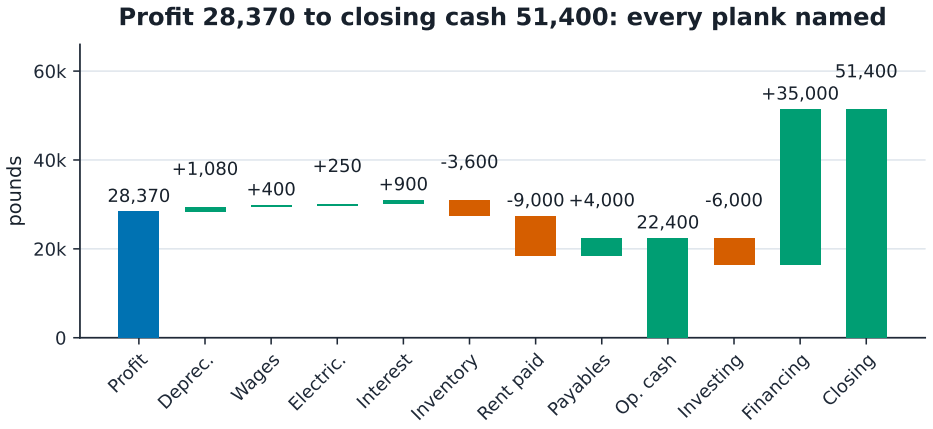
Objective

Classify flows into operating, investing and financing; reconcile profit to operating cash; explain why profit and cash diverge.

1 Key knowledge and worked examples

■ Three classes and a bridge

The **cash flow statement** classifies movements as **operating**, **investing** or **financing**. The indirect bridge adds back depreciation and accruals, then moves working capital: profit becomes operating cash with every divergence engine named.



Profit to cash is a bridge with named planks

■ Worked example. Nimbus year 1

Profit 28,370 + depreciation 1,080 + accruals 1,550 − inventory 3,600 − prepaid rent 9,000 + payables 4,000 = operating 22,400; investing −6,000; financing +35,000; net 51,400 = the balance sheet's cash ✓.

2 Practice

2.1 Classify: (a) £5,000 loan repayment; (b) £900 interest on it; (c) the oven purchase; (d) a £20,000 dividend; (e) flour purchased on credit. [5]

2.2 From Nimbus's bridge, what single plank moves the most cash, and which engine (timing, growth, capital structure) does it belong to? [3]

2.3 Recompute operating cash if Nimbus had held the same year with NO rent prepayment (rent paid monthly, in year). Which planks change? [3]

3 Exam-style questions

3.1 The café of sheet 2.4 (profit 15,145; depreciation 2,125; accruals wages 800, electricity 180, interest 1,250; receivables 6,000; inventory 2,600; prepayment 8,000; equipment bought 9,000; capital 20,000; loan 25,000). Build the full cash flow statement and show it lands on the balance sheet's cash of 38,900. [8]

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3.2 Profit is 15,145 and operating cash is 2,900. Name the engine driving most of the divergence and state one management action that would narrow it. [3]

Solutions

2.1

- (a) Financing. (b) Operating. (c) Investing. (d) Financing. (e) Operating (and no cash moves until paid).

2.2

- The prepaid rent: −9,000, the largest plank.
- Timing engine: cash moved a year ahead of the expense.
- (Growth owns inventory; capital structure owns the 35,000.)

2.3

- Operating cash rises by 9,000 to 31,400.
- The prepayment plank disappears; every other plank is unchanged.
- Cash at the year end becomes 60,400 – same profit, different cash: timing, not performance.

3.1

- Operating: 15,145 + 2,125 + 800 + 180 + 1,250 − 6,000 − 2,600 − 8,000 = 2,900.
- Investing: equipment −9,000.
- Financing: capital +20,000, loan +25,000.
- Net: 2,900 − 9,000 + 45,000 = 38,900.
- Equals the balance sheet's cash ✓ – the statements close against each other.

3.2

- Timing: the 8,000 rent prepayment and 6,000 receivables against the 2,230 of accruals – working capital absorbed 14,000 of cash that profit already counts as earned or matched.
- Narrowing action: invoice café customers on delivery with the 24-day term enforced (receivables 6,000 → near zero releases up to 6,000).
- Or negotiate monthly rent – either act is a timing fix, not a performance one.

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