

# **MBA in Food & Agribusiness**

## Financial Management

*The Statement of Cashflows*  
*(IAS 7)*

# Why important?



## *CFO urges cashflow as new measure*



Blue-chip companies want to end the market's focus on corporate profits and shift attention to narrower measures of performance following the introduction of international accounting standards, according to Jon Symonds, chief financial officer of AstraZeneca, one of the world's leading pharmaceuticals companies .

By Barney Jopson in London Published: April 21 2005 03:00 |

# The Statement of Cashflows

- Overview of the statement of cashflows
- Operating activities
- Investing activities
- Financing activities

# Statement of Cash Flows

Explains the net increase or decrease in cash as seen in the balance sheet

## Current Asset section of Balance sheet

	2008	2007
Cash/Bank	\$100	\$75

### Statement of Cash Flows includes:

Cash

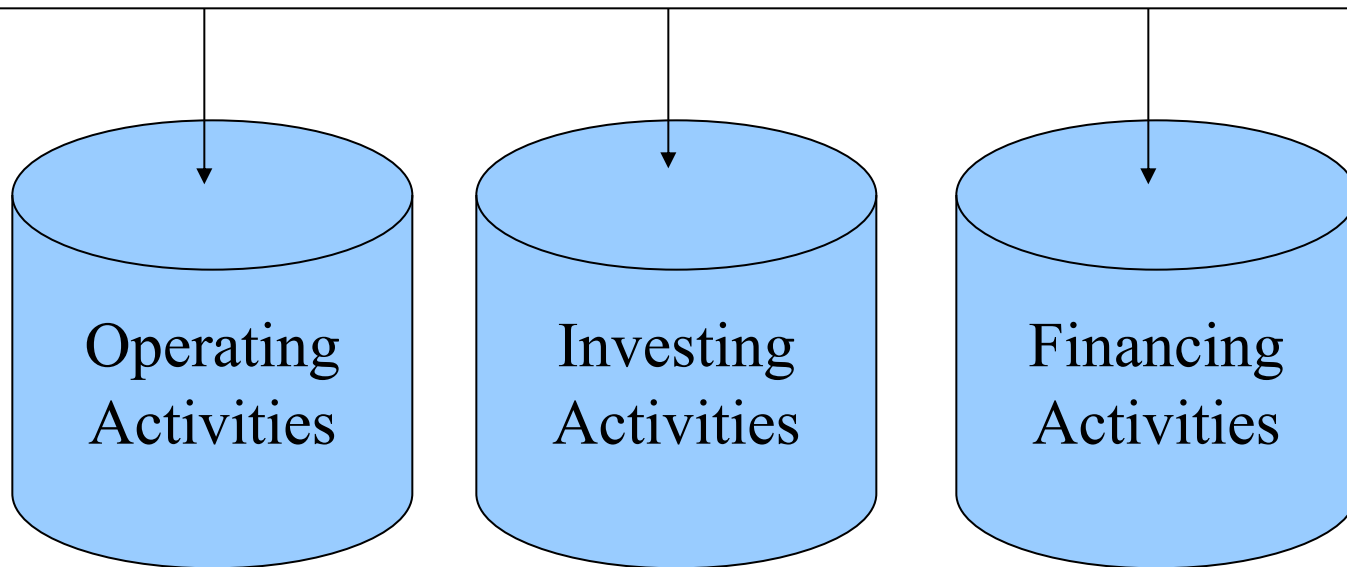
Cash equivalents

- Money market accounts
- Commercial paper
- U.S. Treasury bills



# Classification of Cash Flows

The statement of cash flows classifies cash receipts and cash payments into categories



# Operating Activities

Involve the cash inflows and outflows from activities that enter into the determination of net income

## Cash Inflows

- ✓ Receipts from sale of goods and services
- ✓ Receipts from sale of trading securities
- ✓ Interest and dividends

## Cash Outflows

- ✓ Payments for wages, inventory, expenses, taxes
- ✓ Payments for purchase of trading securities

# Investing Activities

Involve the acquisition and sale of property, plant, and equipment and other long-term assets, including long-term investments

## Cash Inflows

- ✓ Receipts from selling marketable securities and long-term assets
- ✓ Collections on loans

## Cash Outflows

- ✓ Expenditures on purchase of securities and assets
- ✓ Outflows of cash lent to borrowers



# Financing Activities

Obtaining resources from stockholders and providing them with a return on their investments, and obtaining resources from creditors and repaying the amounts borrowed (settling the obligations)

## Cash Inflows

- ✓ Proceeds from stock issues and from short- and long-term borrowing
- ✓ Sales of treasury stock

## Cash Outflows

- ✓ Repayments of loans (excluding interest)
- ✓ Payments to owners, including cash dividends
- ✓ Purchases of treasury stock

# Format of the Statement of Cash Flows – Exhibit

## Marriott International, Inc., and Subsidiaries Consolidated Statement of Cash Flows

	For the Years Ended		
(In millions)	2005	2004	2003
<b>OPERATING ACTIVITIES</b>			
Income from continuing operations	\$ 668	\$ 594	\$ 476
Adjustments to reconcile cash provided by operating activities:			
Income from discontinued operations	1	2	7
Discontinued operations—gain on sale/exit	—	—	19
Depreciation and amortization	184	166	160
Minority interest in results of synthetic fuel operation	(47)	(40)	55
Income taxes	(86)	(63)	(171)
Timeshare activity, net	(6)	113	(111)
Other	160	(77)	(73)
Working capital changes:			
Accounts receivable	(128)	(6)	(81)
Other current assets	(22)	(16)	11
Accounts payable and accruals	113	218	111
<b>Net cash provided by operating activities</b>	<b>\$ 837</b>	<b>\$ 891</b>	<b>\$ 403</b>

# Format of the Statement of Cash Flows (cont.)

<b>INVESTING ACTIVITIES</b>			
Capital expenditures	\$ (181)	\$ (210)	\$ (292)
Dispositions	402	494	729
Loan advances	(129)	(241)	(237)
Loan collections and sales	276	280	124
Other	(81)	(12)	(7)
<b>Cash provided by investing activities</b>	<b>\$ 287</b>	<b>\$ 311</b>	<b>\$ 317</b>
<b>FINANCING ACTIVITIES</b>			
Commercial paper, net	\$ —	\$ (102)	\$ 102
Issuance of long-term debt	20	14	26
Repayment of long-term debt	(99)	(273)	(946)
Redemption of convertible subordinated debt	(62)	—	(347)
Issuance of Class A common stock	206	102	35
Dividends paid	(73)	(68)	(65)
Purchase of treasury stock	(664)	(373)	(252)
Earn-outs received, net	35	17	—
<b>Cash used in financing activities</b>	<b>\$ (637)</b>	<b>\$ (683)</b>	<b>\$ (1,447)</b>
<b>(DECREASE) INCREASE IN CASH AND EQUIVALENTS</b>	<b>\$ 541</b>	<b>\$ 31</b>	<b>\$ (614)</b>
<b>CASH AND EQUIVALENTS, beginning of year</b>	<b>229</b>	<b>198</b>	<b>812</b>
<b>CASH AND EQUIVALENTS, end of year</b>	<b>\$ 770</b>	<b>\$ 229</b>	<b>\$ 198</b>

# Creating the Statement of Cash Flows

- Need Balance Sheet (accrual basis)
- Need Income Statement (accrual basis)

Deduce from Balance sheet and Income statement

**cash receipts or cash payments.**

E.g. Total Sales on credit = \$349,000. Accounts receivable at the beginning of the year is \$ 27,500 and at the end of the year is \$ 23,500 hence cash received from customers is \$ 353,000

# Creating the Statement of Cash Flows – B/S

**Amir Corporation**  
**Comparative Balance Sheets**  
**December 31, 20x8 and 20x7**

	20x8	20x7	Change	Increase or Decrease
<b>Assets</b>				
<b>Current assets</b>				
Cash	\$ 23,000	\$ 7,500	\$ 15,500	Increase
Accounts receivable (net)	23,500	27,500	(4,000)	Decrease
Inventory	72,000	55,000	17,000	Increase
Prepaid expenses	500	2,500	(2,000)	Decrease
<b>Total current assets</b>	<u>\$119,000</u>	<u>\$ 92,500</u>	<u>\$ 26,500</u>	
Investments	\$ 57,500	\$ 63,500	(\$ 6,000)	Decrease
<b>Plant assets</b>				
Plant assets	\$357,500	\$252,500	\$105,000	Increase
Less accumulated depreciation	(51,500)	(34,000)	(17,500)	Increase
<b>Total plant assets</b>	<u>\$306,000</u>	<u>\$218,500</u>	<u>\$ 87,500</u>	
<b>Total assets</b>	<u>\$482,500</u>	<u>\$374,500</u>	<u>\$108,000</u>	
<b>Liabilities</b>				
<b>Current liabilities</b>				
Accounts payable	\$ 25,000	\$ 21,500	\$ 3,500	Increase
Accrued liabilities	6,000	4,500	1,500	Increase
Income taxes payable	1,500	2,500	(1,000)	Decrease
<b>Total current liabilities</b>	<u>\$ 32,500</u>	<u>\$ 28,500</u>	<u>\$ 4,000</u>	
<b>Long-term liabilities</b>				
Bonds payable	147,500	122,500	25,000	Increase
<b>Total liabilities</b>	<u>\$180,000</u>	<u>\$151,000</u>	<u>\$ 29,000</u>	
<b>Stockholders' Equity</b>				
Common stock, \$5 par value	\$138,000	\$100,000	\$ 38,000	Increase
Additional paid-in capital	107,000	57,500	49,500	Increase
Retained earnings	70,000	66,000	4,000	Increase
Treasury stock	(12,500)	0	(12,500)	Increase
<b>Total stockholders' equity</b>	<u>\$302,500</u>	<u>\$223,500</u>	<u>\$ 79,000</u>	
<b>Total liabilities and stockholders' equity</b>	<u>\$482,500</u>	<u>\$374,500</u>	<u>\$108,000</u>	

# Creating the Statement of Cash Flows – I/S

**Amir Corporation**  
**Income Statement**  
**For the Year Ended December 31, 20x8**

Sales		\$349,000
Cost of goods sold		<u>260,000</u>
Gross margin		\$ 89,000
Operating expenses (including depreciation expense of \$18,500)		<u>73,500</u>
Operating income		\$ 15,500
Other income (expenses)		
Interest expense	(\$11,500)	
Interest income	3,000	
Gain on sale of investments	6,000	
Loss on sale of plant assets	<u>(1,500)</u>	<u>(4,000)</u>
Income before income taxes		\$ 11,500
Income taxes expense		<u>3,500</u>
Net income		<u>\$ 8,000</u>

# Determining Cash Flows from Operating Activities

Two methods:

## 1. The direct method

Adjusts each item on the income statement to its cash equivalent

## 2. The indirect method

Lists only necessary adjustments to convert net income to net cash flows

Both methods produce the same net figure

# Depreciation

Expenses appearing in the income statement,  
**but involves no outlay of cash**

Adjustment:  
Depreciation expense  
added back to net  
income  
for the period

Cash flows from operating activities		
Net income		\$8,000
Adjustments to reconcile net income to net cash flows from operating activities		
Depreciation	\$18,500	
Gain on sale of investments	(6,000)	
Loss on sale of plant assets	1,500	
Changes in current assets and current liabilities		
Decrease in accounts receivable	4,000	
Increase in inventory	(17,000)	
Decrease in prepaid expenses	2,000	
Increase in accounts payable	3,500	
Increase in accrued liabilities	1,500	
Decrease in income taxes payable	(1,000)	7,000
<b>Net cash flows from operating activities</b>		<b><u>\$15,000</u></b>



# Gains and Losses

Do not affect cash flows from **operating** activities; should be removed from net income

Adjustments:  
Gain/Losses subtracted  
and added to net income  
for the period

<i>Cash flows from operating activities</i>		
Net income		\$8,000
Adjustments to reconcile net income to net cash flows from operating activities		
Depreciation	\$18,500	
Gain on sale of investments	(6,000)	
Loss on sale of plant assets	1,500	
Changes in current assets and current liabilities		
Decrease in accounts receivable	4,000	
Increase in inventory	(17,000)	
Decrease in prepaid expenses	2,000	
Increase in accounts payable	3,500	
Increase in accrued liabilities	1,500	
Decrease in income taxes payable	(1,000)	<u>7,000</u>
<i>Net cash flows from operating activities</i>		<u>\$15,000</u>

# Changes in Current Assets

Decreases in current assets are added to net income

Increases in current assets are deducted from net income

<b>Accounts Receivable</b>		
Beg. Bal.	27,500	353,000 ← <b>Cash Receipts from Customers</b>
<b>Sales to Customers</b> →	349,000	
End. Bal.	23,500	

The \$4,000 decrease in Accounts Receivable should be added to net income on the statement of cash flows.

# Net Income versus Cash Flows from Operating Activities

Cash flows from operating activities		
Net income		\$8,000
Adjustments to reconcile net income to net cash flows from operating activities		
Depreciation	\$18,500	
Gain on sale of investments	(6,000)	
Loss on sale of plant assets	1,500	
Changes in current assets and current liabilities		
Decrease in accounts receivable	4,000	
Increase in inventory	(17,000)	
Decrease in prepaid expenses	2,000	
Increase in accounts payable	3,500	
Increase in accrued liabilities	1,500	
Decrease in income taxes payable	(1,000)	7,000
Net cash flows from operating activities		<u>\$15,000</u>

# Changes in Current Liabilities

Decreases in current liabilities are deducted from net income

Increases in current liabilities are added to net income

<b>Accounts Payable</b>	
Cash Payments to Suppliers → 273,500	Beg. Bal. 21,500
	277,000 ← Purchases
	End. Bal. 25,000

The \$3,500 increase in Accounts Payable should be added to net income on the statement of cash flows.

# Adjustments for Changes in Current Assets and Liabilities

	<b>Add to Net Income</b>	<b>Deduct from Net Income</b>
<b>Current Assets:</b>		
Accounts receivable (net)	Decrease	Increase
Inventory	Decrease	Increase
Prepaid expenses	Decrease	Increase
<b>Current Liabilities:</b>		
Accounts payable	Increase	Decrease
Accrued liabilities	Increase	Decrease
Income taxes payable	Increase	Decrease

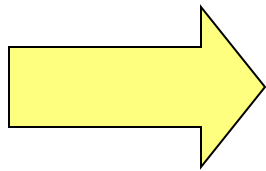
# Net Income versus Cash Flows from Operating Activities

A net income of \$8,000, after adjustments, actually yielded \$15,000 in positive cash flows from operating activities

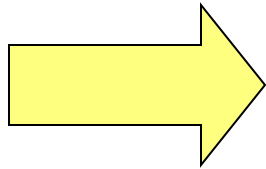
Cash flows from operating activities		
Net income		\$8,000
Adjustments to reconcile net income to net cash flows from operating activities		
Depreciation	\$18,500	
Gain on sale of investments	(6,000)	
Loss on sale of plant assets	1,500	
Changes in current assets and current liabilities		
Decrease in accounts receivable	4,000	
Increase in inventory	(17,000)	
Decrease in prepaid expenses	2,000	
Increase in accounts payable	3,500	
Increase in accrued liabilities	1,500	
Decrease in income taxes payable	(1,000)	7,000
Net cash flows from operating activities		\$15,000

# Examining Investment Transactions

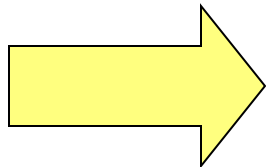
To determine cash flows from investing activities, accounts involving cash receipts and cash payments from investing activities are examined individually



Long-term assets



Short-term investments



Investment gains and losses

# Investment Transactions Cash Flows Illustrated

1. Amir Corporation's purchases of investments totaled \$39,000 during 20x7. These transactions, caused a **\$39,000** decrease in cash flows (cash paid).
2. Amir sold investments that cost \$45,000 for \$51,000. This transaction resulted in a gain of \$6,000 (reported in the income statement) and caused an increase in cash flows of **\$51,000** (cash received) .

Investing activities section, statement of cash flows:

Purchase of investments	(\$39,000)
Sale of investments	51,000



# Plant Asset Transactions Cash Flows Illustrated

1. Amir Corporation purchased plant assets totaling \$60,000. These transactions, caused a **\$60,000** decrease in cash flows (cash paid).
2. Amir sold plant assets that cost \$5,000 and that had accumulated depreciation of \$1,000 for \$2,500. This transaction resulted in a loss of \$1,500 and caused an increase in cash flows of **\$2,500** (cash received) .

Investing activities section, statement of cash flows:

Purchase of plant assets	(\$60,000)
Sale of plant assets	2,500

# Cash Flows from Investing Activities

## **Cash flows from investing activities**

Purchase of investments	(\$39,000)	
Sale of investments	51,000	
Purchase of plant assets	(60,000)	
Sale of plant assets	<u>2,500</u>	
Net cash flows from investing activities		<u>(45,500)</u>

# Noncash Transaction Illustrated

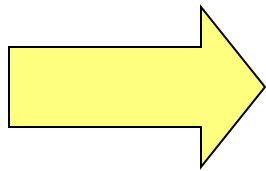
Amir Corporation issued bonds at face value (\$50,000) for plant assets. There are no cash inflows or outflows, but it is a significant transaction.

## Schedule of Noncash Investing and Financing Transactions:

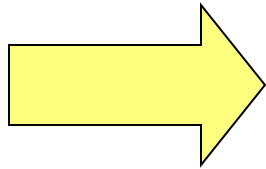
Issue of bonds payable for plant assets     \$50,000

# Examining Financing Transactions

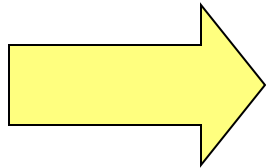
To determine cash flows from financing activities, accounts involving cash receipts and cash payments from financing activities are examined individually



Short-term borrowings



Long-term liabilities



Stockholders' equity

# Bonds Payable Transactions

## Cash Flows Illustrated

Amir Corporation repaid \$25,000 of bonds at face value at maturity. This transaction caused a **\$25,000** decrease in cash flows (cash paid).

Financing activities section, statement of cash flows:

Repayment of bonds      (\$25,000)



# Common Stock Transactions Cash Flows Illustrated

Amir Corporation issued 7,600 shares of \$5 par value common stock for \$87,500. The Common Stock account increased by \$38,000, and the Additional Paid-in Capital account increased by \$49,500. This transaction caused an **\$87,500** increase in cash flows (cash received).

Financing activities section, statement of cash flows:

Issue of common stock	\$87,500
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# Dividend Transactions Cash Flows Illustrated

Amir Corporation **paid** cash dividends in the amount of \$4,000. This amount decreased Retained Earnings. This transaction caused a **\$4,000** decrease in cash flows (cash paid).

Financing activities section, statement of cash flows:

Payment of dividends            (\$4,000)

# Treasury Stock Transactions Cash Flows Illustrated

Amir Corporation purchased treasury stock for \$12,500. This transaction created a cash outflow of \$12,500.

Financing activities section, statement of cash flows:

Purchase of treasury stock      (\$12,500)



# Cash Flows from Financing Activities

<b>Cash flows from financing activities</b>	
Repayment of bonds	(\$25,000)
Issue of common stock	87,500
Payment of dividends	(4,000)
Purchase of treasury stock	<u>(12,500)</u>
Net cash flows from financing activities	<u>46,000</u>

# Statement of Cash Flows

Amir Corporation

Statement of Cash Flows

For the Year Ended December 31, 20x7

Net cash flows from operating activities	\$15,000
Net cash flows from investing activities	(45,500)
Net cash flows from financing activities	46,000
<b>Net increase (decrease) in cash</b>	<u>\$15,500</u>
Cash at beginning of year	7,500
Cash at end of year	<u><u>\$23,000</u></u>