

Analyzing Basket Wonders' Flow of Funds (Sources and Uses of Funds) Statement

Working Capital. The most common meaning is the difference between current assets and current liabilities: **Working capital = current assets - current liabilities**

In this usage, working capital is the dollar amount of current assets left over after the remaining current assets are allocated to pay the company's current liabilities. These “extra” current assets can be used to finance the ongoing work of the business, hence they represent the firm's “working capital.”

Flow of Funds (Sources and Uses of Funds) Statement is a summary of a firm’s changes in financial position from one period to another. How may we use the sources and uses statement in fund and cash-flow analyses and financial planning?

1. Includes important noncash transactions while the cash flow statement does not.
2. Is easy to prepare and often preferred by managers for analysis purposes over the more complex cash flow statement.
3. Helps you to better understand the cash flow statement especially if it is prepared under the “indirect method.”

See the Basket Wonders example below. [Review adjustments in slides 7-14 to 7-21.]

Funds: All of the firm’s investments and claims against those investments. Extends beyond just transactions involving cash.

Assets	2007	2006	+/-	S/U
Cash	\$ 90	\$ 100	\$10	S
Acct. Rec.	394	410	16	S
Inventories	696	616	80	U
Prepaid Exp	5	5	-	-
Accum Tax Prepay	10	9	1	U
Current Assets	\$ 1,195	\$ 1,140		N/A
Fixed Assets (@Cost)	1030	930		N/A
Less: Acc. Depr.	(329)	(299)		N/A
Net Fix. Assets	\$ 701	\$ 631	70	U
Investment, LT	50	50	-	-
Other Assets, LT	223	223	-	-
Total Assets	\$ 2,169	\$ 2,044		

	A	L
S	-	+
U	+	-

S – Sources; U – Uses; A – Assets; L – Liabilities;
+/- increases/decreases in assets or liabilities

“Basic” Sources and Uses Statement

Liabilities and Equity	2007	2006	+/-	S/U
Notes Payable	\$ 290	\$ 295	\$ 5	U
Acct. Payable	94	94	-	-
Accrued Taxes	16	16	-	-
Other Accrued Liab.	100	100	-	-
Current Liab.	\$ 500	\$ 505		N/A
Long-Term Debt	530	453	77	S
Shareholders' Equity				
Com. Stock (\$1 par)	200	200	-	-
Add Pd in Capital	729	729	-	-
Retained Earnings	210	157	53	S
Total Equity	\$ 1,139	\$ 1,086		N/A
Total Liab/Equity	\$ 2,169	\$ 2,044		

Sources	
+ Increase, Retained Earnings	\$ 53
- Decrease, Accounts Receivable	\$ 16
+ Increase, Long-Term Debt	\$ 77
- Decrease, Cash	\$ 10
Total	\$ 156
Uses	
+ Increase, Inventories	\$ 80
+ Increase, Accum Tax Prepay	\$ 1
- Decrease, Notes Payable	\$ 5
+ Increase, Net Fixed Assets	\$ 70
Total	\$ 156

Summary: Basket Wonders Sources and Uses Statement Analysis

Sources: Primarily through net profit from operations and long-term debt increases.

Uses: Primarily through an increase in inventories and expenditures on capital assets.

Analyzing Basket Wonders Statement of Cash Flows

Statement of Cash Flows is a summary of a firm's payments during a period of time. This statement reports cash inflows and outflows based on the firm's operating activities, investing activities, and financing activities. The statement of cash flows provides information about cash flows that is lost when reported only indirectly by the balance sheet and the income statement. The statement of cash flows helps users assess:

- a firm's ability to generate cash.
- a firm's ability to meet its obligations.
- the reasons for differences between income and associated cash flows.
- the effect of cash and noncash investing and financing activities on a firm's financial position.

Cash Flow from Operating activities: Shows impact of transactions not defined as investing or financing activities. These cash flows are generally the cash effects of transaction that enter into the determination of net income.

Cash Inflows

- From sales of goods or services
- From interest and dividend income (*not investing inflow as classified by FASB*)

Cash Outflows

- To pay suppliers for inventory
- To pay employees for services
- To pay lenders (interest)
- To pay government for taxes
- To pay other suppliers for other operating expenses

Cash Flow from Investing Activities: Shows impact of buying and selling fixed assets and debt or equity securities of other entities.

Cash Inflows

- From sale of fixed assets (property, plant, equipment)
- From sale of debt or equity securities (other than common equity) of other entities

Cash Outflows

- To acquire fixed assets (property, plant, equipment)
- To purchase debt or equity securities (other than common equity) of other entities

Cash Flow from Financing Activities: Shows impact of all cash transactions with shareholders and the borrowing and repaying transactions with lenders.

Cash Inflows

- From borrowing
- From the sale of the firm's own equity securities

Cash Outflows

- To repay amounts borrowed
- To repurchase the firm's own equity securities
- To pay shareholders dividends

Two Reporting Formats: We may make adjustments to the statement of cash flows through the direct or indirect methods.

