C) **Cash Flows from financing activities**

Issue of share capital		500	
Long term borrowing		500	
		1000	
Less : Repayment of long term debt (4)	360		
Interest paid (5)	540		
Dividend paid	2,400		
		3,300	
Net cash used in financing activities			(----) 2300
Net increase in cash and cash equivalents			1,500
Add : Cash and cash equivalent at the beginning (Rs. 50 + Rs. 270 Short term Investments)			320
Cash and cash equivalent at the end			1,820*

* [Rs. 400 + (Short term investments Rs. 1340 + Loss in exchange rate Rs. 80)]

Working Notes:

1) **Cash receipts form customers**

	(Rs. in 000)
Sales	61,300
Add : Sundry debtors at the beginning	2,400
	63,700
Less : Sundry debtors at the end	3,400
	60,300

2) **Cash paid to suppliers and employees**

		(Rs. in 000)
Cash of Sales		52,000
Administrative and selling expenses		1,820
		53,820
Add : Opening creditors	3,780	
" Inventories at the end	1,800	5,580
		59,400
Less : Creditors at the end	300	
" Opening inventories	3,900	4,200
		55,200

3) **Income tax paid**

	(Rs. in 000)
Tax paid (Including Tax deducted at source from dividends received)	600
Add : Tax liability at the beginning	2,000
	2600
Less : Tax liability at the end	800
	1,800

Out of Rs.1800, tax deducted at source on dividends received (Rs.80), is shown in 'Cash Flows from Investing Activities' and balance of Rs. 1720 is to be shown under 'cash flows from operating activities'.

4) **Repayment of long term borrowings**

	(Rs. in 000)
Long term debt at the beginning	2,080
Add : Long term debt made during the year	500
	2,580
Less : Long term debt at the end	2,220
	360

5) **Interest Paid**

		(Rs. in 000)
	Interest expense for the year	800
Add :	Interest Payable at the beginning	200
		1,000
Less :	Interest payable at the end	460
		540

Cash Flow Statement (Indirect Method)

			(Rs. in 000)
Cash flows from operating activities			**2005 year**
Net Profit before taxation and extraordinary item			6,700
Adjustments for:			
	+ Depreciation	900	
	+ Foreign exchange loss	80	
	+ Interest expense	800	
	--- Interest income	(---) 600	
	--- Dividend income	(---) 400	780
Operating Profit before Working Capital Changes			7480
(---)	Increase in sundry debtors	(---) 1,000	
(+)	Decrease in inventories	2,100	
(---)	Decrease in sundry creditors	(---) 3,480	(---) 2,380
	Cash Generated from Operations		5,100
(---)	Income tax paid (Rs. 1800 --- Tax deducted at source Rs. 80)		1,720
	Cash flow before extraordinary item		3,380
	Proceeds from earthquake settlement		360
	Net Cash from Operating Activities		3,740
Cash flows from investing activities			
(---)	Fixed assets purchased	(---) 700	
(+)	Proceeds from sale of plant	40	
(+)	Interest received (Interest income Rs. 600 --- Accrued interest Rs. 200)	400	
(+)	Dividend received (Rs. 400 --- Tax deducted at source Rs. 80)	320	
	Net Cash from Investing Activities		60
Cash flows from financing activities			
(+)	Issue of additional capital	500	
(+)	Proceeds from long term borrowings	500	
(---)	Repayment of long term borrowings (Opening balance Rs. 2,080 + Borrowings during the year Rs. 500 --- Balance at the end Rs. 2,220)	(---) 600	
(---)	Interest paid	(---) 540	
(---)	Dividend paid	(---) 2,400	(---) 2,300
Net Cash Used in Financing Activities			1,500
Cash & Cash equialent at the beginning (Rs. 50 + Rs. 270)			320
Cash and cash equivalent at the end			1,820

20.10 USES OF CASH FLOW STATEMENT

Cash flow statement is very useful to the financial management. It is used as a tool for financial analysis for short term planning.

The preparation of cash flow statement has several uses. The more important uses are as follows:

1) Changes in cash balance between two points of time and the contributing factors for such change are clearly revealed.

2) The cash flow statement explains the reasons for:

   i) the presence of very low cash balance inspite of huge operating profits: or

   ii) the presence of a higher cash balance inspite of a very low level of profits

3) Projected cash fow statements help the management in short-term planning and several other ways like:

   i) Determination of additional cash requirements during a given period and making timely arrangements

   ii) Identification of the size of surplus and the time for which such surplus funds are likely to be available

   iii) Judging the ability of the firm to repay/redeem debentures/preferences shares.

   iv) Examining the possibility of maintaining/increasing dividends

   v) Assessing the capability of finance, replacement of fixed assets

   vi) Assessing the capacity of the firm to finace expansion.

   vii) More efficient and effective management of cash flows.

20.11 DISTINCTION BETWEEN CASH FLOW ANALYSISAND FUND FLOWANALYSIS

Following are the major points of difference between cash flow analysis and fund flow analysis:

1) Fund flow analysis deals with the change in working capital position between two balance sheet dates, whereas the cash flow analysis is concerned with the change in cash position.

2) Cash flow analysis is more useful as a tool in short-term financial planning, whereas fund flow analysis is more useful in long-term financial planning.

3) An increase in current liability or decrease in current asset (other than cash) results in an increase in cash whereas such changes result in decrease in the net working capital. Similarly, a decrease in any current liability or an increase in current asset (other than cash) results in a decrease in cash, whereas such changes increase the net working capital.

4) Cash flow statement recognises 'cash basis of accounting' where as funds flow statement is based on accrual basis of accounting.

5) Cash flow analysis explains only the causes of cash variations, wheresas funds flow analysis discloses the causes of overall working capital variations.

Activity 6

1) Compute the changes in cash flow from operating activities of Infosys between Year 2001 & 2000 and 2002 & 2001.

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2) Compute the changes in profit before taxes and depreciation of Infosys between Year 2001 & 2000 and 2002 & 2001.

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3) Compare whether the profit changes are in line with the changes in cash flow from operating activities.

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4) Repeat the above two steps for few companies and write your findings.

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20.12 LET US SUM UP

Cash Flow Statement and cash flow analysis have assumed importance particularly when many companies have started adopting creative accounting and earnings management. Realising the needs of new users as well as others, regulating agencies have made reporting of cash flow statements mandatory. Cash flow statement is easy to understand and difficult to manipulate. It provides three important pieces of information on cash flow movements of the firm --- how much cash is generated through operation, financing and how much cash is spent for investment? It gives a clear and real picture about the internal activities of the firm. There are two methods of preparation of cash flow statements, namely direct and indirect method. While direct method gives more details on cash flow from operating activities and also reader-friendly, indirect method is more accounting oriented and fails to provide any additional information. Unfortunately, many companies use indirect method though the accounting standards allow both methods. This indirectly shows the eagerness of management to withhold information unless it is required by the regulation. Fortunately, the final figure is adequate to get good insight though additional information will always be useful. Cash flow analysis are typically done by comparing the changes in cash flow from operating activities from period to period with the changes in profit levels of the firm. Such comparison is useful to understand the quality of reported profit. Also, the cash flow from operating activities are used to compare whether they are sufficient to meet the liabilities of lenders and also contribute for further investments.

20.13 KEY WORDS

Cash Flow: Movement of cash i.e., cash in flow and cash outflow

Cash Flow Statement: Statement prepared to show the sources and uses of cash between the two balance sheets dates.

Cash from Operations: Net profit adjusted for changes in the current items in additional to the adjustments already made while ascertaining funds from operations.

20.14 TERMINAL QUESTIONS

1) How cash flow statement is different from income statement? What are the additional benefits to different users of accounting information from cash flow statement?
2) List down any four important accounting transactions that increase the profit but has no impact on cash flow statement.
3) How does cash flow statement differ from funds flow statement? What are the uses of cash flow statement?
4) How does cash flow analysis help the management in decision making?
5) What is a 'Cash Flow Statement'? Explain the techniques of preparing a cash flow statement.
6) A summary of Cash Flow Statement of Shaheed Industries Ltd. for the last few years is given below. The details of profit are also stated. Suppose you are an analyst working for a leading mutual fund in India prepare a small report on the performance of the company using these two pieces of information.

Summary of Cash Flow Statement of Shaheed Industries Ltd.

Year	**2003**	**2002**	**2001**	**2000**
Cash and Cash Equivalents at Beginning of the year	1,760.71	143.27	1,081.55	4,897.60
Cash from Operating Activities	6,642.31	7,523.00	4,748.08	1,630.55
Cash Used In Investing Activities	-6,575.53	-3,928.34	-2,423.89	-5,000.06
Cash Used In Financing Activities	-1,680.28	-1,977.22	-3,305.11	-446.54
Net Inc/(Dec) In Cash And Cash	-1,613.50	1,617.44	-980.92	-3,816.05
Cash and Cash Equivalents at end of the Year	147.21	1,760.71	100.63	1,081.55
Net Profit Before tax & Extraordinary Items	4,974.21	4,428.70	2,645.62	2,403.25
Depreciation	3,452.79	3,435.82	2,636.73	2,533.59

7) The following are the Balance Sheet of M/s. Rao Brother Private Ltd. as on March 2004 and 2005

Liabilities	**2004 Rs.**	**2005 Rs.**	**Assets**	**2004 Rs.**	**2005 Rs.**
Equity Shares	4,000	4,000	Fixed assets	4,100	4,000
12% Redeenable			Less : Depreciation	1,100	1,500
Preference shares	----	1,000		3,000	2,500
Profit and loss a/c	100	120	Sundry Debtors	2,000	2,400
General reserve	200	200	Stock	3,000	3,500
Debentures	600	700	Prepaid expenses	30	50
Creditors	1,200	1,100	Cash	120	350
Provision for taxation	800	1,000			
Bank overdraft	1,250	680			
	8,150	8,800		8,150	8,800

Your are required to prepare a Cash Flow Statement.

(**Ans.** Cash from Operation Rs. 400, Sources Rs.1,600, Applications Rs. 800)