

Cash Flow	Statement of Cash Flows: Direct ("Top-down")
<p>Cash Flow more important than Profit (Net Income)</p> <ul style="list-style-type: none"> necessary to pay bills (including taxes) and exploit growth opportunities consistent with wealth maximization (dividends are paid in cash) unambiguous (can't be manipulated) <p>Statement of Cash Flows flow of actual cash through firm during period includes cash flows from Operations, Investment, Financing</p> <p>Operating Cash Flow analogous to Net Income, but excludes non-cash income/expenses (and interest)</p> <p>Investment Cash Flows purchase/sale of fixed assets and marketable securities interest and dividends received</p> <p>Financing Cash Flow some consider interest paid an operating cash flow</p>	<p>Requires detailed information Similar to Income Statement, but with all non-cash items filtered out</p> <ul style="list-style-type: none"> Cash Collected from Customers Cash Paid to Suppliers Cash Operating Expenses (Selling & Administration) Taxes = Cash Flow from Operating Activities + Cash Received from Sales of Assets - Cash Paid to Purchase Assets + Interest Received from Loans to Others + Dividends Received from Other Firm's Stock = Cash Flow from Investment Activities + Cash Received from Selling New Securities - Repayment of Debt (Principal) - Retirement/Repurchase of Firm's Own Stock - Interest Paid on Firm's Own Debt - Dividends Paid on Firm's Own Stock = Cash Flow from Financing Activities = Net Cash Flow
3/2017, page 1	3/2017, page 2

Reminder: Sources and Uses of Cash	Statement of Cash Flows: Indirect ("Bottom-Up")									
<p>Sources provide inflows Decrease in assets, e.g., sell fixed or current assets Increase in claims (liability or equity), e.g., take out bank loan, sell new securities</p> <p>Uses provide outflows Increase in assets, e.g., purchase fixed or current assets Decrease in claims (liability or equity), e.g., pay off bank loan, repurchase/retire securities</p> <table border="1" style="margin: 10px auto;"> <thead> <tr> <th></th> <th style="text-align: center;">Assets</th> <th style="text-align: center;">Claims</th> </tr> </thead> <tbody> <tr> <td>Source (inflow)</td> <td style="text-align: center;">↓</td> <td style="text-align: center;">↑</td> </tr> <tr> <td>Use (outflow)</td> <td style="text-align: center;">↑</td> <td style="text-align: center;">↓</td> </tr> </tbody> </table> <p>End-of-Period Cash Balance = Beginning-of-Period Cash Balance + Cash Inflows - Cash Outflows</p>		Assets	Claims	Source (inflow)	↓	↑	Use (outflow)	↑	↓	<p>Most commonly used ("Reconciliation") Requires Income Statement and 2 Balance Sheets</p> <ul style="list-style-type: none"> Net Income + Depreciation - Change in Accounts Receivable - Change in Inventories + Change in Accounts Payable - Change in Accruals = Cash Flow from Operating Activities Change in Marketable Securities Change in (Gross) Fixed Assets + Interest Received from Loans to Others + Dividends Received from Other Firm's Stock = Cash Flow from Investment Activities + Change in Long-term Debt + Sale of New Stock - Retirement/Repurchase of Firm's Own Stock - Interest Paid on Firm's Own Debt - Dividends Paid on Firm's Own Stock = Cash Flow from Financing Activities = Net Cash Flow
	Assets	Claims								
Source (inflow)	↓	↑								
Use (outflow)	↑	↓								
3/2017, page 3	3/2017, page 4									

Ambiguity: Net Income v. Operating Cash Flow						
Depreciation Method	Straight-Line		Accelerated			
	Income Statement	Cash?	Cash Flow Statement	Income Statement	Cash?	Cash Flow Statement
Sales (all cash)	1000	Y	1000	1000	Y	1000
Costs (all cash)	700	Y	(700)	700	Y	(700)
Depreciation	100		-200			
EBIT	200		100			
Interest	0		0			
EBT	200		100			
Taxes: 40%	80	Y	(80)	40	Y	(40)
NI	120		60			
Depreciation	100		-200			
Cash Flow	220		220	260		260

When depreciation increases, NI falls but OCF rises.
Though depreciation is not itself a cash flow, it reduces taxes.
Interest is a cash flow, but from financing, not operations. It also reduces taxes.

Calculating Operating Cash Flow (OCF), alternative	Free Cash Flow (FCF)
<p>Alternative "bottom-up approach," starting with EBIT</p> <p>OCF = EBIT - Taxes + Depreciation = 200 - 80 + 100 = 220 (straight-line) or = 100 - 40 + 200 = 260 (accelerated)</p> <p>This works since, from the Income Statement,</p>	<p>Definition Cash flow actually available to investors, after deducting an allowance for investments in assets (fixed and current) necessary to maintain the income stream into the future Payment will not impair future operations</p> <p>Where it comes from</p> <p>where means "change in," and</p>
3/2017, page 5	3/2017, page 6

Cash Flows to Investors
<p>Where it goes Cash flow paid out of Free Cash Flow to investors, both creditors (bondholders and other lenders) and owners (shareholders)</p> <p>where</p> <p>and</p> <p>Summary</p>
3/2017, page 9

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