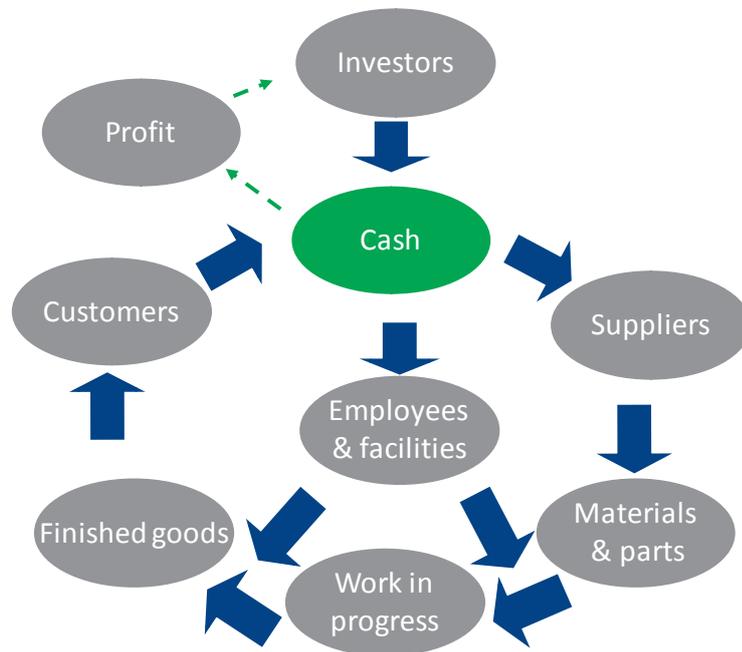**The Cash Flow Cycle Explained**

Start at the top of the diagram, with investors, and work round following the arrows.

Initially cash is required to start a business and this comes from investors such as share holders and lenders e.g. banks. This can be supplemented by the credit facilities offered by suppliers.

The cash is used to buy materials and parts from suppliers and to buy facilities and employ staff.

The employees perform the process and turn materials and parts into finished goods, which are sold to the customer.

In a non manufacturing organisation the majority of the cash is paid out on employees and facilities as supposed to materials and the customers pay for the service they receive.

The cash then returns into the business. If the incoming cash exceeds the outgoing cash then a profit is made.

The profit is actually realised in the accounts at the point when the goods are invoiced as this is the point when the sales are logged into the accounts. This is usually sooner than the cash appears in the bank, the true point at which cash returns into the business.

The profit is used to pay dividends or interest to the investors and/or is retained as profit to fund the business.

The objective for the organisation is to complete the cash flow cycle as quickly as possible i.e. from receipt of materials and parts to receiving the payment from the customer.

All the steps in between represent risk to the organisation as it needs actual cash to survive; the inventory cannot be used to pay the wages and bills.

Buying materials and holding stock, producing too many parts, producing scrap, shipping parts incorrectly, customers cancelling orders or going out of business are all risks incurred by the organisation.

The longer the lead time through the cash flow cycle the greater the risk.

The desired outcome therefore is to move cash through the cycle more quickly, in smaller amounts. This reduces the level of risk to the business and provides a smoother and more stable cash flow.