



## A conceptual study of fund flow statement

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### Abstract

A statement of fund flow is created in order to assess the factors behind changes in a company's financial status from one balance sheet to another. It illustrates the movement of money in and out, showing where the funds come from and how they are used during a specific timeframe. It is equally appropriate to mention that a cash flow statement is created to clarify the alterations in the company's working capital status. The necessity arises because the profit and loss and balance sheet do not provide insight into the reasons for a shift in the financial status. The profit and loss account and balance sheet will show the financial figures for two years: the current year and the previous year. However, it will not provide an explanation for why the shift occurred, such as the increased utilization of long-term funds for long-term purposes and the utilization of short-term funds for both short-term and long-term needs. This is the reason for preparing the fund flow statement. This article is a humble effort to examine the necessity and significance of a Fund Flow Statement.

**Keywords:** Financial management, fund flow statement, working capital

### Introduction

At the end of a time frame, it is customary to prepare a profit and loss statement and a financial statement to provide a brief summary of all economic transactions during that period. However, the income statement has limitations as it only considers the funds coming in and going out in relation to the sale of goods or services. In the same way, financial management involves overseeing the movement of money generated by business choices and deals, while the balance sheet provides a quick view of the assets and debts at a particular time. The goal is to manage the actions intentionally and in a positive manner for the company's advantage. Hence, it is essential to record, scrutinize, and clarify the changes in the organization's economic condition and oversee future endeavors. Transfer of funds corresponds to any changes in current assets. These changes occur non-stop, on a daily basis, with each transaction taking place. Hence, changes in working capital may be called 'flow'. Working capital may come in or go out, referred to as either 'inflow' or 'outflow'.

It is crucial to eliminate the non-fund based adjustments to focus solely on changes that involve the flow of funds. Nevertheless, the profit figure for the fund flow statement should include income earned but not received and expenses incurred but not paid that are accounted for in the profit and loss statement. Fund flow statements are helpful in pinpointing various operational issues within a company. Companies that use short-term funds for long-term investments could face liquidity issues down the road. In the meantime, if a company is using long-term funds to support short-term ventures, it may not be effectively leveraging its capital.

### Components of a fund flow statement

A Fund Flow Statement has two main components: sources of funds and uses of funds. It helps in identifying how businesses raise funds and how they are utilized.

#### Sources of funds

- Issue of shares, debentures
- Loans (long-term)

- Sale of assets
- Funds from operations: Funds generated from business activities, adjusted for non-cash transactions like depreciation.

#### Uses of funds

- Purchase of assets
- Loan repayment
- Dividend payments
- Changes in working capital

Understanding these components helps businesses manage their working capital and make informed financial decisions.

### Prepare a fund flow statement

Preparing a Fund Flow Statement involves several key steps:

- 1. Statement of Changes in Working Capital:** Identify the differences in current assets and liabilities.
- 2. Funds from Operations:** Determine the funds generated from core operations, adjusting for non-cash items.
- 3. Statement of Sources and Uses of Funds:** Summarize the movement of funds and the impact on working capital.

The Fund Flow Statement is typically prepared using balance sheet and income statement data. Businesses rely on it for long-term financial planning, tracking trends, and managing cash flow effectively.

### Need of fund flow statement

- 1. Demonstrates the Company's Financial Status:** A fund flow statement provides insight into the different origins and applications of funds. It also highlights the differences in financial status between two distinct balance sheet dates. Therefore, it outlines the financing and investment activities of the company.

2. **Provides information on total funds raised:** It indicates the portion of funds raised from the sale of fixed assets, issuance of shares or debentures, long-term or short-term loans, and day-to-day company activities.
3. Ensures transparency in funds usage by providing specifics on their explicit utilization. This involves the amount spent on acquiring fixed assets and settling tax payments, dividends, and other responsibilities. It also explains the amount used for the redemption of preferred shares, debentures, or short-term loans.
4. **Shows cash flow in and out:** It helps management to show all cash inflows and outflows impacting a company's working capital.
5. **Assists with financial and performance management:** The anticipated cash flow statement helps managers maintain oversight of the company's finances and investment outlays. Fund flow statements are employed by management to evaluate the financial and operational performance of the company.

#### **Importance of fund flow statement for financial management**

Monitoring and controlling working capital is crucial for businesses, with a cash flow statement being a critical financial tool. Listed below are several purposes for which financial analysts and managers choose to utilize the Funds Flow Statement.

#### **Significance of analysis in financial transactions**

While the financial statements display the assets and their usage, they do not explain the causes behind the Balance Sheet changes. The statement offers an analytical perspective on the distinctions between current assets and current liabilities. Therefore, it also clarifies the process by which these changes occur within the financial resources of a company that is impacted. In some situations, despite the company making a profit, there may still be instances of cash shortages. In these situations, this statement offers a transparent view of the organization's earnings.

#### **Aids in creating a successful dividend strategy**

At times, a company may have a large amount of profit that can be given out as dividends, but struggles to do so because of a shortage of liquidity. A Funds Flow Statement can pinpoint liquidity restrictions and aid in developing a successful dividend policy.

#### **Functions as a financial advisor**

This statement also acts as a financial advisor for a company. It highlights the potential financial challenges that a company may encounter soon. The management can therefore devise a suitable plan to safeguard the company against potential future financial setbacks.

#### **Assists in evaluating the financial reliability of a company**

Lending institutions frequently choose to review this statement over a number of years to determine the creditworthiness of a company before granting a loan. Therefore, it also demonstrates the reliability of a company in managing funds.

#### **Limitations of funds flow statement**

- Despite having various crucial features, financial analysts face certain challenges with the Funds Flow Statement, highlighting its limitations for use.
- This statement is unable to depict the financial data shown in a Balance Sheet or Income Statement. It solely examines the transfer of money within a set period and does not measure other crucial factors.
- The statement does not contribute any additional numerical worth to a company's financial position. It simply reorganizes the existing data to detect problems in managing funds.
- Because of its historical context, this statement does not accurately reflect the current financial position of a business.
- Working capital is crucial in finance for businesses. Nevertheless, the flow of money is crucial for the successful financial prospects of a company. Therefore, the movement of money is not a reliable indicator for the intention.

Nevertheless, despite the constraints of this assertion, it assists financial analysts in assessing the balance sheet and making recommendations for efficient fund management. Therefore, it is essential for all organizations, both small and large, to be aware of their fund flow in order to make better financial choices.

#### **Concluding remarks**

The company is thriving as a result of the increasing success in both the international and local markets. It is a new one with creative and inventive ideas and focuses on enhancing all aspects of its operations. The company maintains a strong liquidity position and promptly fulfills its financial obligations to both creditors and debtors. Because the company heavily relies on working capital facilities, it maintains strong relationships with its vendors and effectively manages its working capital. The liquidity of the company should improved by maintaining the optimum current assets and liquid assets according to standard norms. In order to improve the financial health of the company and maximizing the time between the funds mobilization and utilization, the management must introduce the new cost saving techniques. It is concluded the overall performance of the organisation is satisfactory.

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