



# PROJECT CASH FLOW

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- Basic Principles of Cash Flow Estimation
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# INTRODUCTION

“It is an accounting term that refers to the amounts of cash being received and spent by a business during a defined period of time, sometimes tied to a specific project.”

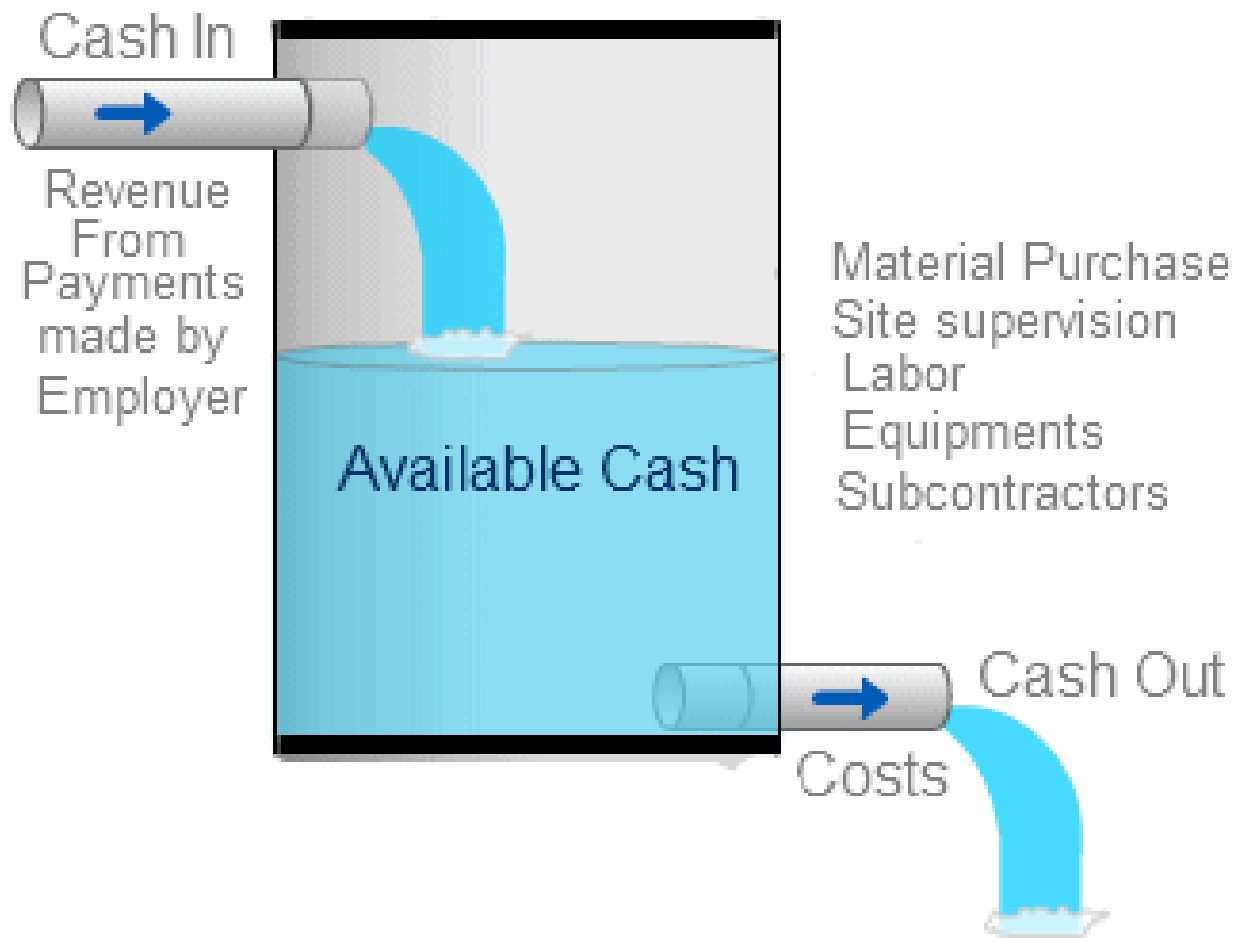
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## CASH FLOW PROJECTION

The projection of income and expense during the life of a project can be developed from several time-scheduling aids used by the contractor.

# Elements of The Cash Flow Stream

## Contractor Cash Flow



## CASH INFLOWS

CASH SALES  
RECEIPTS FROM TRADE  
SALE OF SPARE ASSETS  
INVESTMENT OF SHARE  
CAPITAL  
PERSONAL FUNDS  
INVESTED  
RECEIPT OF BANK LOAN  
GOVERNMENT GRANTS  
RECEIPTS FROM  
FACTORING

## CASH OUTFLOWS

PAYMENT OF WAGES &  
SALARIES  
PAYMENT OF SUPPLIERS  
BUYING EQUIPMENT  
INTEREST ON BANK  
LOAN OR OVERDRAFT  
PAYEMENT OF  
DIVIDENDS  
PAYMENT OF LOANS  
PAYMENT OF LEASING  
OR HIRE PURCHASE  
RENTALS  
INCOME TAX , VAT &  
CORPORATION TAX

# Elements of The Cash Flow Stream

- A project which involves cash outflows followed by cash inflows comprises of three basic components. They are,
  - Initial investment: Initial investment is the after-tax cash outlay on capital expenditure and net working capital when the project is set up.
  - Operating cash inflows: The operating cash inflows are the after-tax cash inflows resulting from the operations of the project during its economic life.
  - Terminal cash inflow: The terminal cash inflow is the after-tax cash flow resulting from the liquidation of the project at the end of its economic life.

# Basic Principles of Cash Flow Estimation

- The following principles should be followed while estimating the cash flows of a project:
  - Incremental principle
  - Separation principle
  - Post-tax principle
  - Consistency principle.

# Basic Principles of Cash Flow Estimation

## Incremental principle:

- The cash flow of a project must be measured in incremental terms.
- To ascertain a project's incremental cash flow one has to look at what happens to the cash flows of the firm **with** the project and **without** the project.
- The difference between the two reflects the incremental cash flows attributable to the project .



# Basic Principles of Cash Flow Estimation

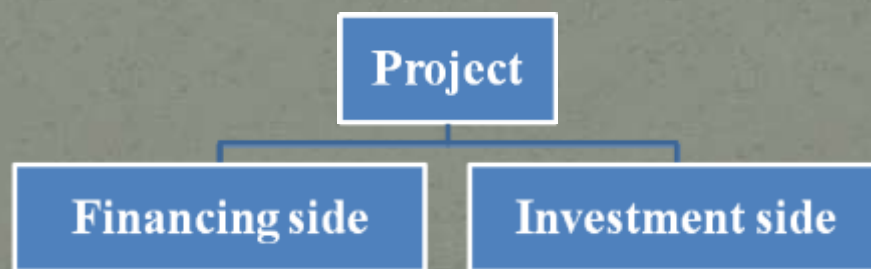
## Incremental principle:

- In estimating the incremental cash flows of a project, the following guidelines must be borne in mind:
  - Consider all incidental effects.
  - Ignore sunk costs.
  - Include opportunity costs.
  - Question the allocation of overhead costs.
  - Estimate working capital properly

# Basic Principles of Cash Flow Estimation

## Separation principle

- There are two sides of a project:
  - The investment (or asset) side
  - The financing side
- The cash flows associated with these sides should be separated.



# Basic Principles of Cash Flow Estimation

## Post-tax principle

- Cash flow should be measured on an after-tax basis.
- This is used to bring out the project cash flows with accuracy.

## Consistency principle

- Once you adopt an accounting principle or method, you should continue to follow it consistently in future accounting periods.

# Cash flows relating to long term funds

- The cash flow stream relating to long-term funds consists of three components as follows:
  - Initial investment: Long-term funds invested in the project. This is equal to:  
Fixed assets + working capital margin (this represents the portion of current assets supported by long-term funds)
  - Operating cash inflow:  
Profit after tax + Depreciation + Other noncash charges + Interest on long-term borrowings (1-tax rate)
  - Terminal cash flow:  
Net salvage value of fixed assets + Net recovery of working capital margin

# Cash flows relating to long term funds

- Initial investment = Fixed assets + working capital margin
- Operating cash inflow = Profit after tax + Depreciation + Other noncash charges + Interest on long-term borrowings (1-tax rate)
- Terminal cash flow = Net salvage value of fixed assets + Net recovery of working capital margin

THANK YOU