

Cash Management

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Learning Objectives



By the end of this chapter, participants will be able to:

- ✓ Define cash and cash management
- ✓ Explain the importance of effective cash management
- ✓ Identify reasons for holding cash
- ✓ Distinguish cash from profit and working capital
- ✓ Explain the cash-management cycle
- ✓ Prepare a cash budget
- ✓ Forecast cash receipts and payments
- ✓ Calculate cash surpluses and financing gaps
- ✓ Determine an appropriate minimum cash balance
- ✓ Explain cash-collection and disbursement systems
- ✓ Evaluate short-term investment alternatives
- ✓ Assess short-term financing options
- ✓ Explain cash-management models
- ✓ Identify major cash risks and internal controls
- ✓ Recommend strategies for improving cash performance



Chapter Roadmap

01

Meaning of cash management

02

Importance of cash

03

Motives for holding cash

04

Cash versus profit

05

Cash-flow cycle

06

Cash forecasting

07

Cash budgeting

08

Minimum cash balances

09

Cash collections

10

Cash disbursements

11

Surplus-cash investment

12

Short-term financing

13

Cash-management models

14

Bank-account management

15

Cash controls and fraud prevention

16

Cash-performance indicators



What Is Cash?

Cash includes financial resources available for immediate use. It may include:

- Cash on hand
- Petty cash
- Bank balances
- Demand deposits
- Mobile-money balances
- Highly liquid cash equivalents



What Is Cash Management?

Cash management is the process of:

- Planning cash requirements
- Forecasting cash flows
- Collecting cash efficiently
- Controlling payments
- Maintaining adequate liquidity
- Investing temporary surpluses
- Financing temporary shortages
- Protecting cash from fraud and loss



The Central Cash-Management Question

“

How much cash should an organization hold, when will it be needed, and how should temporary surpluses or shortages be managed?

Cash management exists to answer this question.



Objectives of Cash Management

The principal objectives are to:

- Meet obligations when due
- Avoid unnecessary idle cash
- Minimize financing costs
- Accelerate cash collections
- Control cash payments
- Invest surplus funds safely
- Maintain financial flexibility
- Protect organizational resources



Cash as the Most Liquid Asset

Cash is the most liquid asset because it can be used immediately to:

- Pay suppliers
- Pay employees
- Settle taxes
- Repay debt
- Purchase inventory
- Finance emergencies
- Support daily operations



Cash Is Essential but Low-Yielding

Cash provides liquidity but usually generates a low return. Excess cash carries an opportunity cost — the funds could be:

- Invested
- Used to repay debt
- Used for expansion
- Used to purchase productive assets
- Distributed to owners

IMPORTANT

Holding excessive cash creates an opportunity cost.



Cash-Management Goal

“

The goal is not to maximize cash — it is to hold enough to operate safely, without so much that resources remain unproductive.

Balance liquidity against return.



Operational Continuity

Effective cash management ensures the organization can:

- Pay salaries
- Purchase supplies
- Maintain service delivery
- Meet loan obligations
- Pay taxes
- Respond to emergencies
- Avoid operational interruption



Liquidity Management

Liquidity is the ability to meet financial obligations when they become due. Cash management is therefore central to:

- Short-term solvency
- Creditor confidence
- Supplier relationships
- Financial stability

KEY IDEA

Liquidity keeps the organization able to pay what it owes, on time.



Cash and Organizational Survival

A profitable organization may fail if it cannot generate cash at the right time. Possible causes include:

- Slow customer collections
- Excess inventory
- Large debt repayments
- Heavy capital expenditure
- Poor cash forecasting
- Rapid growth

IMPORTANT

Profit is not the same as survival — timing of cash matters.



Cash and Growth

Growth often requires additional cash for:

- Inventory
- Receivables
- Staff
- Facilities
- Marketing
- Technology
- Operating expenses

IMPORTANT

Rapid growth may increase cash pressure before extra revenue is collected.



Cash and Risk Management

Strong cash management reduces:

- Payment-default risk
- Emergency borrowing
- Supplier disruption
- Penalties
- Interest costs
- Fraud exposure
- Financial distress



Cash and Reputation

Timely payment supports:

- Supplier confidence
- Employee trust
- Lender relationships
- Government compliance
- Investor confidence
- Organizational credibility



Main Motives for Holding Cash

1

Transaction

To meet normal operational payments.

2

Precautionary

To protect against unexpected events.

3

Speculative

To seize favourable opportunities.

4

Compensating

Minimum balances required by banks.

5

Regulatory

Contractual or statutory requirements.



Transaction Motive

Cash is held to meet normal operational payments. Examples include:

- Payroll
- Supplier invoices
- Rent
- Utilities
- Transport
- Taxes
- Loan repayments



Precautionary Motive

Precautionary cash protects against unexpected events. Examples include:

- Delayed receivables
- Emergency purchases
- Revenue shortfalls
- Equipment breakdown
- Market disruption
- Natural disaster



Speculative Motive

Cash may be retained to take advantage of opportunities such as:

- Supplier discounts
- Asset purchases
- Market-price declines
- Investment opportunities
- Emergency procurement
- Acquisition opportunities



Compensating Balance

“

A compensating balance is a minimum bank balance required as part of a financing or banking arrangement.

It may reduce the amount of cash effectively available for use.



Regulatory and Contractual Cash

Some organizations are required to maintain cash because of:

- Loan agreements
- Donor conditions
- Regulatory capital requirements
- Insurance conditions
- Reserve policies
- Board-approved minimum balances



Cash Is Not the Same as Profit

“

Profit is an accounting measure; cash reflects actual receipts and payments. A company may report profit without receiving cash immediately.

Accrual profit and cash timing diverge.



Why Profit and Cash Differ

Differences may arise from:

- Credit sales
- Depreciation
- Accrued expenses
- Prepaid expenses
- Inventory purchases
- Capital expenditure
- Loan transactions
- Tax timing



Profit without Cash — Example

A company makes a credit sale of ETB 1 million. The sale may increase:

- Revenue
- Profit
- Accounts receivable

EXAMPLE

But cash does not increase until the customer actually pays.



Cash without Profit — Example

“

**A company receives a bank loan of ETB 5 million.
Cash increases — but the loan is not revenue or
profit; it creates a liability.**

Financing inflows are not income.



Cash vs Net Working Capital

$$\text{Net Working Capital} = \text{Current Assets} - \text{Current Liabilities}$$

Cash is only one component of current assets. A company may have positive working capital but limited immediate cash.



Cash Flow vs Accounting Income

Cash Flow

- Based on receipts and payments
- Focuses on liquidity
- Includes financing flows
- Essential for payment capacity

Accounting Income

- Based on accrual accounting
- Focuses on profitability
- Excludes most financing receipts
- Essential for performance measurement



Main Cash-Flow Categories

1

Operating

Cash from core, day-to-day activities.

2

Investing

Cash for and from long-term assets.

3

Financing

Cash from owners and lenders.



Operating Cash Flows

Operating cash flows arise from core activities.

Inflows

- Customer collections
- Service fees
- Grant receipts for operations
- Other operating receipts

Outflows

- Suppliers
- Salaries
- Utilities
- Taxes
- Operating expenses



Investing Cash Flows

Investing activities include:

- Purchase of equipment
- Purchase of buildings
- Sale of fixed assets
- Purchase of long-term investments
- Proceeds from investment sales



Financing Cash Flows

Financing activities include:

- Loan proceeds
- Loan repayments
- Equity contributions
- Share issuance
- Dividends
- Lease financing
- Bond issuance



Positive and Negative Cash Flow

Positive Cash Flow

- Cash inflows exceed cash outflows

Negative Cash Flow

- Cash outflows exceed cash inflows

A temporary negative cash flow may be manageable if it is planned and financed.



The Cash Cycle

01

Cash

02

Purchases and
operating costs

03

Inventory or service
delivery

04

Sales

05

Receivables

06

Cash collection



Cash Conversion Cycle

$$\text{CCC} = \text{Inventory Days} + \text{Receivables Days} - \text{Payables Days}$$

The cash conversion cycle measures how long cash remains committed to operations.



Shortening the Cash Cycle

Cash can be recovered faster by:

- Reducing inventory days
- Accelerating invoicing
- Improving collections
- Negotiating longer supplier terms
- Reducing processing delays
- Using electronic payments



Cash-Flow Timing

“

Cash management is concerned not only with the total amount of cash but also with its timing.

An organization may have sufficient annual revenue yet still face monthly cash shortages.



What Is Cash Forecasting?

Cash forecasting estimates future:

- Cash receipts
- Cash payments
- Opening balances
- Closing balances
- Financing gaps
- Temporary surpluses



Importance of Cash Forecasting

Cash forecasts help management to:

- Anticipate shortages
- Arrange financing early
- Invest temporary surpluses
- Schedule payments
- Avoid idle balances
- Support decision-making
- Monitor financial risk



Cash-Forecast Horizons

Cash forecasts may cover:

- Daily periods
- Weekly periods
- Monthly periods
- Quarterly periods
- Annual periods
- Multi-year strategic periods



Short-Term Cash Forecast

A short-term forecast focuses on:

- Immediate receipts
- Payroll
- Supplier payments
- Taxes
- Debt service
- Bank balances

KEY IDEA

It supports daily liquidity decisions.



Medium-Term Cash Forecast

A medium-term forecast may cover 3–12 months. It supports:

- Budget implementation
- Procurement planning
- Financing decisions
- Seasonal cash requirements
- Capital-expenditure scheduling



Long-Term Cash Forecast

Long-term forecasting supports:

- Strategic planning
- Capital investment
- Debt-capacity analysis
- Expansion
- Financing structure
- Sustainability assessment



Forecasting Methods

Cash may be forecast using:

- Receipts-and-payments method
- Adjusted-net-income method
- Balance-sheet method
- Historical trends
- Scenario analysis
- Rolling forecasts



Receipts-and-Payments Method

“

This method lists expected cash inflows and outflows by period.

It is especially useful for short-term cash planning.



Adjusted-Net-Income Method

This method begins with forecast profit and adjusts for:

- Non-cash expenses
- Working-capital changes
- Capital expenditure
- Financing flows
- Taxes
- Other cash items



Rolling Cash Forecast

“

A rolling forecast is updated continuously — each month a new future month is added so the forecast always covers the next 12 months.

Forecasting never stops; it rolls forward.



What Is a Cash Budget?

A cash budget is a detailed estimate of expected cash inflows and outflows over a defined period. It shows:

- Opening cash
- Receipts
- Payments
- Net cash flow
- Closing cash
- Financing need
- Surplus cash



Cash-Budget Structure

$$\text{Closing Cash} = \text{Opening Cash} + \text{Cash Receipts} - \text{Cash Payments}$$

Every cash budget rests on this identity.



Main Cash Receipts

Cash receipts may include:

- Cash sales
- Collection of receivables
- Loan proceeds
- Grant receipts
- Investment income
- Asset-sale proceeds
- Owner contributions
- Tax refunds



Main Cash Payments

Cash payments may include:

- Inventory purchases
- Salaries
- Rent
- Utilities
- Taxes
- Debt service
- Capital expenditure
- Dividends
- Insurance
- Administrative expenses



Cash-Budget Example

$$\text{Closing} = \text{Opening} + \text{Receipts} - \text{Payments}$$

WHERE

- Opening cash: ETB 1,000,000
- Cash receipts: ETB 5,000,000
- Cash payments: ETB 5,600,000

WORKING

- $\text{Closing} = 1,000,000 + 5,000,000 - 5,600,000$

RESULT

Closing Cash = ETB 400,000



Minimum Cash Requirement

Assume the minimum required cash balance is ETB 800,000.

$$\text{Financing Need} = \text{Minimum Balance} - \text{Closing Cash}$$

WORKING

- = 800,000 – 400,000

RESULT

Financing Need = ETB 400,000



Cash Surplus

$$\text{Surplus Cash} = \text{Closing Cash} - \text{Minimum Cash Balance}$$

If closing cash exceeds the minimum required balance, the surplus may be invested or used to repay short-term debt.



Monthly Cash Budget

Item	Month 1	Month 2	Month 3
Opening cash	X	X	X
Cash receipts	X	X	X
Cash payments	(X)	(X)	(X)
Net cash flow	X	X	X
Closing cash	X	X	X
Financing or surplus	X	X	X

Template structure — replace X with forecast values for each month.



Cash-Budget Decision Use

A cash budget allows management to decide:

- When to borrow
- How much to borrow
- When to repay
- When to invest surplus funds
- Which payments can be scheduled
- Whether operations are financially feasible



Collection Patterns

Cash collections depend on:

- Cash sales
- Credit-sales percentage
- Customer-payment behavior
- Credit terms
- Collection efficiency
- Bad-debt experience
- Seasonal trends



Collection Schedule Example

Assume credit sales are collected as follows:

- 20% in the month of sale
- 60% in the following month
- 20% in the second month after sale

KEY IDEA

Cash receipts should be forecast using these collection patterns.



Collection Example

Credit sales:

- January: ETB 1,000,000
- February: ETB 1,200,000
- March: ETB 1,500,000

EXAMPLE

March collections = 20% of March + 60% of February + 20% of January sales.



Calculate March Collections

$$\text{March} = 20\%(\text{Mar}) + 60\%(\text{Feb}) + 20\%(\text{Jan})$$

WORKING

- $20\% \times 1,500,000 = \text{ETB } 300,000$
- $60\% \times 1,200,000 = \text{ETB } 720,000$
- $20\% \times 1,000,000 = \text{ETB } 200,000$

RESULT

Total = ETB 1,220,000



Collection Forecast Risks

Forecast errors may arise from:

- Customer delays
- Disputes
- Bad debts
- Economic downturn
- Weak invoicing
- Incorrect sales forecasts
- Currency restrictions



Payment Patterns

Cash payments depend on:

- Supplier credit terms
- Payroll schedules
- Tax dates
- Loan agreements
- Capital-expenditure plans
- Insurance schedules
- Rent and lease terms



Supplier Payment Forecast

Suppose purchases are paid:

- 30% in the month of purchase
- 70% in the following month

KEY IDEA

Payments should be scheduled based on forecast purchases and supplier terms.



Payroll Forecast

Payroll forecasts should include:

- Basic salary
- Allowances
- Pension
- Taxes
- Bonuses
- Overtime
- Temporary staff
- Employer contributions



Debt-Service Forecast

Debt-service forecasts should show:

- Interest
- Principal
- Fees
- Balloon payments
- Lease installments
- Currency effects
- Maturity dates



Capital-Expenditure Payments

Capital-expenditure payments may occur through:

- Advance payment
- Progress payments
- Delivery payment
- Retention payment
- Final settlement

KEY IDEA

Timing should reflect contract terms.



What Is a Minimum Cash Balance?

“

A minimum cash balance is the amount the organization intends to maintain for operational and risk purposes.

It is a deliberate safety floor, not idle money.



Factors Affecting Minimum Cash

The minimum balance depends on:

- Payment volatility
- Collection reliability
- Access to credit
- Business risk
- Operating scale
- Banking arrangements
- Emergency needs
- Management risk appetite



Minimum Cash Policy

A cash policy may define the minimum balance as:

- A fixed amount
- A percentage of monthly expenses
- A number of operating days
- A percentage of annual expenditure
- A risk-based reserve



Days-of-Cash Formula

$$\text{Days of Cash} = \text{Available Cash} \div \text{Average Daily Cash Operating Cost}$$

It expresses liquidity as the number of days the organization can operate on current cash.



Days-of-Cash Example

$$\text{Days of Cash} = \text{Available Cash} \div \text{Daily Operating Cost}$$

WHERE

- Available cash: ETB 3,000,000
- Annual cash operating costs: ETB 36,000,000

WORKING

- Daily cost = $36,000,000 \div 365 \approx \text{ETB } 98,630$
- Days = $3,000,000 \div 98,630$

RESULT

≈ 30.4 days



Excessive Minimum Balance

An excessively high minimum balance may result in:

- Idle funds
- Lower returns
- Higher opportunity cost
- Reduced investment
- Unnecessary borrowing elsewhere

COMMON MISTAKE

Too much reserve wastes earning capacity.



Inadequate Minimum Balance

An inadequate cash reserve may lead to:

- Payment delays
- Emergency borrowing
- Penalties
- Supplier disruption
- Financial distress
- Reduced operational flexibility

COMMON MISTAKE

Too little reserve threatens solvency.



Objectives of Collection Management

Collection management seeks to:

- Receive cash promptly
- Reduce collection delays
- Minimize bad debts
- Improve liquidity
- Reduce banking float
- Strengthen customer accountability



Collection Techniques

Organizations may use:

- Electronic invoicing
- Bank transfers
- Mobile payments
- Direct debit
- Standing orders
- Online-payment portals
- Collection agents
- Lockbox systems



Electronic Invoicing

Electronic invoicing can:

- Reduce preparation time
- Improve delivery speed
- Reduce errors
- Enable automated reminders
- Improve recordkeeping
- Accelerate collection



Early-Payment Discounts

An organization may offer a discount for early payment.

2 / 10, net 30

The customer receives a 2% discount if payment is made within 10 days; otherwise the full amount is due in 30 days.



Evaluating Early-Payment Discounts

Management should compare:

- Faster cash collection
- Reduced bad-debt risk
- Cost of the discount
- Financing-cost savings
- Customer response
- Administrative impact



Collection Follow-Up

A collection process may include:

1. Invoice delivery confirmation
2. Reminder before due date
3. Follow-up on due date
4. Escalation for overdue balances
5. Payment-plan negotiation
6. Credit suspension
7. Legal action



Receivables Aging

Receivables aging classifies outstanding amounts by age.

Category	Management Response
Current	Routine monitoring
1–30 days overdue	Reminder
31–60 days overdue	Formal follow-up
61–90 days overdue	Escalation
Above 90 days	Recovery or legal action



Objectives of Payment Management

Disbursement management seeks to:

- Pay valid obligations on time
- Avoid unnecessary early payments
- Capture supplier discounts
- Prevent duplicate payments
- Maintain internal control
- Preserve cash safely



Payment Timing

Organizations should normally pay:

- On the agreed due date
- Earlier when discounts are financially attractive
- Later only when formally agreed

COMMON MISTAKE

Unapproved payment delay may damage supplier relationships.



Payment Prioritization

When cash is limited, payments may be prioritized based on:

- Legal obligations
- Payroll
- Taxes
- Critical suppliers
- Debt service
- Essential operations
- Contractual penalties
- Strategic importance



Centralized Disbursement

Centralized payment systems may provide:

- Better control
- Improved cash visibility
- Reduced duplicate payments
- Stronger authorization
- Better bank negotiations



Decentralized Disbursement

Decentralized payment may provide:

- Faster local response
- Operational flexibility
- Reduced processing delays

KEY IDEA

It also requires strong controls and reporting.



Payment Scheduling

A payment schedule should identify:

- Supplier
- Invoice
- Due date
- Amount
- Discount opportunity
- Approval status
- Funding source
- Payment priority



What Is Float?

“

Float is the difference between the cash balance shown in the organization's records and the balance shown by the bank.

It arises from timing differences.



Collection Float

Collection float is the delay between:

- Customer payment
- Receipt of funds
- Bank processing
- Availability of cash



Disbursement Float

Disbursement float is the delay between:

- Issuing payment
- Supplier presentation
- Bank processing
- Reduction in available funds



Components of Float

Float may include:

- Mailing time
- Processing time
- Bank clearing time
- Deposit availability time
- Internal approval delay



Reducing Collection Float

Collection float can be reduced through:

- Electronic payments
- Direct bank deposits
- Mobile payments
- Lockbox services
- Faster invoice issuance
- Automated reconciliation



Ethical Use of Disbursement Float

Organizations should not deliberately issue payments without sufficient funds. Payment timing should remain:

- Contractually compliant
- Transparent
- Ethical
- Supported by available cash

IMPORTANT

Never issue payments without sufficient funds.



What Is Surplus Cash?

Surplus cash is cash available above:

- Immediate operational needs
- Minimum reserve
- Expected near-term payments
- Restricted-fund requirements



Objectives of Short-Term Investment

Temporary surplus cash should be invested with emphasis on:

1. Safety
2. Liquidity
3. Maturity matching
4. Return

IMPORTANT

Safety and liquidity normally take priority over high return.



Short-Term Investment Alternatives

Possible alternatives include:

- Bank deposits
- Treasury bills
- Money-market instruments
- Short-term government securities
- High-quality commercial paper
- Money-market funds
- Repurchase agreements

KEY IDEA

Availability depends on local markets and organizational policy.



Investment Selection Criteria

Management should consider:

- Credit quality
- Liquidity
- Maturity
- Return
- Currency
- Marketability
- Legal restrictions
- Counterparty risk
- Transaction costs



Maturity Matching

“

Investment maturity should match the expected date when cash will be required.

Funds needed in one month should not be locked into a long-term investment.



Restricted Cash

Restricted funds should only be invested or used in accordance with:

- Donor agreements
- Loan conditions
- Legal requirements
- Board policy
- Contractual restrictions



Cash Shortage

A cash shortage occurs when expected available cash falls below the minimum required balance. Management must decide how to:

- Reduce payments
- Accelerate receipts
- Use reserves
- Obtain short-term financing
- Reschedule activities



Short-Term Financing Sources

Possible sources include:

- Bank overdraft
- Short-term loan
- Revolving credit
- Trade credit
- Factoring
- Invoice discounting
- Internal reserves
- Intercompany financing



Bank Overdraft

A bank overdraft provides flexible financing up to an agreed limit.

Advantages

- Flexible use
- Interest on amount used
- Suitable for temporary shortages

Risks

- Variable interest
- Repayable on demand
- Renewal uncertainty



Short-Term Loan

A short-term loan provides a defined amount for a specified period. Management should consider:

- Interest rate
- Fees
- Collateral
- Repayment period
- Covenants
- Effective annual cost



Trade Credit

Supplier credit delays cash payment for purchases.

Benefits

- Spontaneous financing
- Limited formal documentation
- Support for operations

Costs

- Lost discounts
- Higher prices
- Supplier dependence
- Late-payment penalties



Factoring

Factoring converts receivables into immediate cash by selling them to a financial institution. It may:

- Improve liquidity
- Reduce collection time
- Transfer some credit risk
- Create financing and service costs



Financing Decision Criteria

Short-term financing should be evaluated based on:

- Cost
- Flexibility
- Availability
- Maturity
- Collateral
- Risk
- Currency
- Impact on relationships
- Administrative requirements



Purpose of Cash Models

Cash-management models help determine appropriate transfers of funds.

Transfers Between

- Cash
- Marketable securities
- Short-term investments

They Balance

- Transaction costs
- Opportunity costs
- Liquidity needs



Baumol Cash Model

The Baumol model applies an inventory-style approach to cash. It assumes:

- Cash usage is predictable
- Cash outflows occur steadily
- Funds can be transferred from investments
- Transaction and opportunity costs are known



Baumol Formula

$$C^* = \sqrt{(2FT \div i)}$$

WHERE

- C^* = optimal cash transfer amount
- F = transaction cost per conversion
- T = total cash required for the period
- i = opportunity cost of holding cash



Baumol Example

$$C^* = \sqrt{(2FT \div i)}$$

WHERE

- Annual cash requirement (T): ETB 12,000,000
- Transaction cost (F): ETB 500
- Annual opportunity cost (i): 10%

WORKING

- $C^* = \sqrt{(2 \times 500 \times 12,000,000 \div 0.10)}$



Baumol Solution

$$C^* = \sqrt{120,000,000,000}$$

WORKING

- Evaluate the square root

RESULT

$C^* \approx \text{ETB } 346,410$

INTERPRETATION

The organization would transfer about ETB 346,410 each time, under the model assumptions.



Average Cash Balance under Baumol

$$\text{Average Cash Balance} = C^* \div 2$$

WORKING

- = $346,410 \div 2$

RESULT

≈ ETB 173,205



Limitations of the Baumol Model

The model may be unsuitable when:

- Cash flows are highly uncertain
- Receipts occur frequently
- Payments are irregular
- Bank access is limited
- Transaction costs vary
- Minimum balances are required



Miller–Orr Model

The Miller–Orr model is designed for uncertain cash flows. It establishes:

- Lower cash limit
- Upper cash limit
- Target return point

KEY IDEA

Cash is allowed to fluctuate within a control range.



Miller–Orr Decision Rule

At the Upper Limit

- Surplus cash is invested
- Cash returns to the target level

At the Lower Limit

- Investments are sold
- Cash returns to the target level



Miller–Orr Advantages

The model:

- Recognizes uncertainty
- Reduces unnecessary transfers
- Maintains a control range
- Supports flexible cash decisions



Bank-Account Objectives

Bank accounts should support:

- Secure custody
- Efficient collection
- Controlled payments
- Accurate reporting
- Reconciliation
- Fund segregation
- Regulatory compliance



Bank-Account Structure

Organizations may use:

- Main operating account
- Payroll account
- Project accounts
- Foreign-currency accounts
- Collection accounts
- Investment accounts
- Petty-cash accounts



Too Many Bank Accounts

Excessive bank accounts may create:

- Idle balances
- Higher fees
- Weak oversight
- Reconciliation delays
- Fraud risk
- Complex reporting

COMMON MISTAKE

More accounts can mean weaker control.



Bank Reconciliation

Bank reconciliation compares:

- Cash book
- Bank statement
- Outstanding payments
- Deposits in transit
- Bank charges
- Interest
- Errors



Bank-Reconciliation Formula

$$\text{Adjusted Bank Balance} = \text{Adjusted Cash-Book Balance}$$

All reconciling items should be investigated and cleared promptly.



Common Reconciliation Items

Reconciling items may include:

- Outstanding cheques
- Deposits in transit
- Bank charges
- Direct deposits
- Standing orders
- Interest income
- Recording errors
- Unauthorized transactions



Bank Signatories

Bank-signatory controls should define:

- Authorized signatories
- Approval limits
- Number of signatures required
- Electronic approval rules
- Temporary delegation
- Periodic review



What Is Petty Cash?

Petty cash is a small amount held for minor and urgent expenses. Examples include:

- Local transport
- Small office supplies
- Minor repairs
- Postage
- Emergency incidental costs



Imprest System

Under an imprest system:

- A fixed petty-cash amount is established
- Payments are supported by vouchers
- The fund is replenished for the amount spent
- The fund returns to its authorized balance



Petty-Cash Controls

Controls should include:

- Approved fund limit
- Designated custodian
- Sequential vouchers
- Supporting receipts
- Spending limits
- Surprise counts
- Regular replenishment
- No personal use



Petty-Cash Reconciliation

Cash on Hand + Approved Vouchers = Authorized Petty-Cash Float

Any difference must be investigated.



Major Cash Risks

Cash risks include:

- Theft
- Fraud
- Unauthorized payment
- Duplicate payment
- Misappropriation
- Bank error
- Cybercrime
- Foreign-exchange loss
- Liquidity shortage
- Counterparty failure



Fraud Risks

Cash fraud may involve:

- Fictitious payments
- Altered payment instructions
- False suppliers
- Payroll fraud
- Unauthorized withdrawals
- Skimming
- Lapping
- Duplicate invoices



Cyber and Payment Fraud

Electronic-payment risks include:

- Phishing
- Business-email compromise
- Account takeover
- Malware
- False bank-detail changes
- Unauthorized system access



Foreign-Currency Risk

Foreign-currency cash may gain or lose value from exchange-rate movements. Management should monitor:

- Currency exposure
- Payment currency
- Conversion timing
- Restrictions
- Hedging opportunities



Counterparty Risk

Counterparty risk is the possibility that a bank or investment institution fails to meet its obligations. Risk can be reduced through:

- Approved-bank lists
- Credit-quality limits
- Diversification
- Exposure limits
- Regular monitoring



Core Cash Controls

Strong cash controls include:

- Segregation of duties
- Authorization
- Documentation
- Reconciliation
- Physical security
- Restricted system access
- Independent review
- Audit trails



Segregation of Duties

Different individuals should be responsible for:

- Authorizing transactions
- Recording transactions
- Holding cash
- Preparing payments
- Approving payments
- Reconciling accounts



Payment Authorization

Payments should require:

- Valid obligation
- Approved budget
- Supporting documents
- Appropriate coding
- Authorization within limits
- Confirmed supplier details
- Evidence of receipt



Three-Way Matching

Before payment, compare:

1. Purchase order
2. Goods-received note
3. Supplier invoice

KEY IDEA

This confirms the transaction is valid and accurate.



Supplier Bank-Detail Changes

Changes to supplier bank details should require:

- Independent verification
- Formal written request
- Callback to a verified contact
- Management approval
- System audit trail

COMMON MISTAKE

A frequent target of payment fraud — always verify.



Daily Cash Controls

Daily controls may include:

- Recording all receipts
- Depositing collections promptly
- Reviewing bank balances
- Matching receipts to invoices
- Securing cash
- Reviewing unusual transactions



Monthly Cash Controls

Monthly controls may include:

- Bank reconciliation
- Cash-flow variance analysis
- Petty-cash count
- Bank-fee review
- Signatory review
- Restricted-cash reconciliation
- Outstanding-item follow-up



Key Cash Indicators

Useful indicators include:

- Days of cash on hand
- Operating cash-flow ratio
- Cash ratio
- Cash conversion cycle
- Forecast accuracy
- Collection period
- Payment period
- Financing cost
- Idle-cash balance



Cash Ratio

$$\text{Cash Ratio} = (\text{Cash} + \text{Cash Equivalents}) \div \text{Current Liabilities}$$

It measures the ability to cover current liabilities using only the most liquid assets.



Operating Cash-Flow Ratio

$$\text{Operating Cash-Flow Ratio} = \text{Operating Cash Flow} \div \text{Current Liabilities}$$

It measures the extent to which operating cash flow covers short-term obligations.



Cash Forecast Accuracy

$$\text{Forecast Variance} = \text{Actual Cash Flow} - \text{Forecast Cash Flow}$$

Regular variance analysis helps improve forecasting.



Collection Efficiency

Collection performance may be monitored using:

- Receivables days
- Overdue percentage
- Aging distribution
- Collection rate
- Bad-debt ratio
- Promise-to-pay compliance



Idle-Cash Indicator

$$\text{Idle Cash} = \text{Actual Available Cash} - \text{Required Operational Cash}$$

Persistent idle balances may indicate weak treasury management.



Daily Cash Report

A daily cash report may show:

- Bank balances
- Cash on hand
- Expected receipts
- Planned payments
- Available liquidity
- Restricted funds
- Short-term borrowing
- Exceptions



Weekly Cash Report

A weekly report may include:

- Opening liquidity
- Actual receipts
- Actual payments
- Closing liquidity
- Forecast for next four weeks
- Financing gap
- Investment opportunity
- Major risks



Cash Dashboard

A management dashboard may display:

- Total cash
- Unrestricted cash
- Restricted cash
- Days of cash
- Overdue receivables
- Short-term debt
- Forecast variance
- Minimum-balance compliance



Cash-Flow Variance Analysis

Variance analysis should identify whether differences arise from:

- Timing
- Volume
- Price
- Delayed collections
- Unplanned payments
- Forecasting errors
- Exchange-rate movements



Practical Exercise — Prepare and Evaluate a Cash Budget

In this exercise, participants will:

- Forecast cash receipts
- Forecast cash payments
- Calculate monthly closing balances
- Identify financing needs
- Identify cash surpluses
- Recommend borrowing or investment actions
- Evaluate cash risks

EXERCISE

Work through the scenario on the following slides.



Exercise Scenario

Opening cash (January): ETB 500,000 · Minimum required cash: ETB 400,000

Month	Projected Sales
January	ETB 1,000,000
February	ETB 1,200,000
March	ETB 1,500,000



Collection Assumptions

Sales are collected as follows:

- 30% in the month of sale
- 50% in the next month
- 20% in the second month

EXAMPLE

December sales: ETB 800,000. November sales: ETB 700,000.



January Cash Collections

$$\text{Jan} = 30\%(\text{Jan}) + 50\%(\text{Dec}) + 20\%(\text{Nov})$$

WORKING

- $30\% \times 1,000,000 = 300,000$
- $50\% \times 800,000 = 400,000$
- $20\% \times 700,000 = 140,000$

RESULT

Total = ETB 840,000



February Cash Collections

$$\text{Feb} = 30\%(\text{Feb}) + 50\%(\text{Jan}) + 20\%(\text{Dec})$$

WORKING

- $30\% \times 1,200,000 = 360,000$
- $50\% \times 1,000,000 = 500,000$
- $20\% \times 800,000 = 160,000$

RESULT

Total = ETB 1,020,000



March Cash Collections

$$\text{Mar} = 30\%(\text{Mar}) + 50\%(\text{Feb}) + 20\%(\text{Jan})$$

WORKING

- $30\% \times 1,500,000 = 450,000$
- $50\% \times 1,200,000 = 600,000$
- $20\% \times 1,000,000 = 200,000$

RESULT

Total = ETB 1,250,000



Projected Cash Payments

Month	Projected Payments
January	ETB 1,100,000
February	ETB 900,000
March	ETB 1,300,000



January Closing Cash

$$\text{Closing} = \text{Opening} + \text{Collections} - \text{Payments}$$

WHERE

- Opening: ETB 500,000
- Collections: ETB 840,000
- Payments: ETB 1,100,000

WORKING

- $\text{Closing} = 500,000 + 840,000 - 1,100,000 = \text{ETB } 240,000$
- Minimum required = ETB 400,000

RESULT

Financing Need = ETB 160,000



January Financing

“

Borrow ETB 160,000 to restore the minimum balance.

January closing cash after financing: ETB 400,000.



February Closing Cash

$$\text{Closing} = \text{Opening} + \text{Collections} - \text{Payments}$$

WHERE

- Opening: ETB 400,000
- Collections: ETB 1,020,000
- Payments: ETB 900,000

WORKING

- Closing = 400,000 + 1,020,000 – 900,000 = ETB 520,000
- Surplus = 520,000 – 400,000

RESULT

Surplus = ETB 120,000



February Decision

The ETB 120,000 surplus may be used to:

- Repay part of January borrowing
- Maintain an additional reserve
- Invest temporarily



March Closing Cash

Assuming February closes at the minimum balance after debt repayment.

$$\text{Closing} = \text{Opening} + \text{Collections} - \text{Payments}$$

WORKING

- $\text{Closing} = 400,000 + 1,250,000 - 1,300,000 = \text{ETB } 350,000$
- Minimum required = ETB 400,000

RESULT

Financing Need = ETB 50,000



Cash-Budget Summary

Month	Closing Before Financing	Financing Need or Surplus
January	ETB 240,000	Borrow ETB 160,000
February	ETB 520,000	Surplus ETB 120,000
March	ETB 350,000	Borrow ETB 50,000

Cash-flow timing is uneven: shortages in January and March, a temporary surplus in February.



Exercise Interpretation

The company experiences:

- A January cash shortage
- A February temporary surplus
- A March shortage
- Uneven cash-flow timing
- A need for flexible short-term financing



Sensitivity Exercise

Recalculate the cash budget if:

- Customer collections are delayed by one month
- March sales fall by 20%
- January payments increase by ETB 200,000
- Minimum cash rises to ETB 600,000
- A loan installment of ETB 300,000 is due in March

EXERCISE

Test how sensitive liquidity is to each change.



Group Recommendation

Each group should present:

1. Monthly cash collections
2. Monthly closing balances
3. Financing requirement
4. Surplus-investment decision

1. Main cash risks
2. Collection improvements
3. Payment-control improvements
4. Final liquidity recommendation



Common Cash-Management Mistakes

Frequent mistakes include:

- Confusing profit with cash
- Failing to prepare cash forecasts
- Holding excessive idle cash
- Ignoring payment timing
- Delaying invoicing
- Weak collection follow-up
- Paying suppliers unnecessarily early
- Using short-term financing for permanent needs
- Failing to reconcile bank accounts
- Weak segregation of cash duties



Cash-Management Checklist

Management should regularly review:

- Daily cash position
- Minimum cash requirement
- Cash forecast
- Cash-budget variance
- Receivables aging
- Payment schedule
- Bank reconciliations
- Restricted cash
- Short-term investments
- Short-term debt
- Foreign-currency exposure
- Bank-signatory controls
- Cash-fraud indicators



Knowledge Check

Test your understanding:

1. What is cash management?
2. Why do organizations hold cash?
3. How does cash differ from profit?
4. What is a cash budget?
5. How is closing cash calculated?

1. What is a minimum cash balance?
2. How can collections be accelerated?
3. What is float?
4. What priorities apply when investing surplus cash?
5. Why is bank reconciliation important?



Knowledge Check — Answers

#	Answer
1	Planning and controlling cash receipts, payments, surpluses and shortages
2	For transactions, precautions, opportunities and contractual requirements
3	Profit is accrual-based; cash reflects actual receipts and payments
4	A forecast of cash inflows, outflows and balances
5	Opening cash plus receipts minus payments
6	The minimum cash maintained for operations and risk protection
7	Faster invoicing, electronic payment and stronger follow-up
8	Timing difference between recorded and bank cash balances
9	Safety, liquidity, maturity matching and return
10	It identifies errors, unrecorded items and unauthorized transactions



Action Plan

Evaluate your organization's cash-management system by identifying:

- Current available cash
- Restricted and unrestricted balances
- Minimum required cash
- Days of cash available
- Main collection delays
- Major payment obligations
- Short-term financing sources
- Temporary investment options
- Bank-reconciliation status
- Major control weakness
- Immediate corrective action
- Long-term improvement



Chapter Summary

Key lessons from this chapter:

- Cash is essential for meeting immediate obligations
- Cash management balances liquidity, risk and return
- Cash is held for transaction, precautionary and speculative purposes
- Profit and cash are different measures
- Cash forecasting identifies future shortages and surpluses
- Cash budgets support borrowing, payment and investment decisions
- Faster collections improve liquidity
- Controlled payment timing preserves cash without harming relationships
- Temporary surpluses should emphasize safety and liquidity
- Temporary shortages require cost-effective financing
- Bank reconciliation and segregation of duties are fundamental controls
- Strong cash management improves resilience, efficiency and sustainability



Key Message

“

Cash management is not simply about keeping money in a bank account — it is the coordinated management of cash across the whole organization.

Forecasting → Collections → Payments → Minimum Reserves → Short-Term Financing → Surplus Investment → Internal Control → Financial Sustainability

THANK YOU

Questions and Discussion

Effective cash management ensures that financial resources are available when needed without remaining unnecessarily idle. It strengthens liquidity by accelerating collections, controlling disbursements, forecasting shortages and protecting every cash transaction through disciplined internal controls.

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