

I'm making a profit why isn't there anything in the bank?

There can be a big difference between the profit you make and what you end up with in actual cash.

Key reasons for cash to be lower than your profits:

- ✚ Increases in amounts owed to you by your customers (debtors). Your profit is based on sales regardless of whether or not you have been actually paid.
- ✚ Increases in stock (inventory). When calculating your profit the cost of goods actually sold are used not what you purchased. The difference between what you purchased and the cost of the goods you sold will be reflected in changes in the level of stock you hold.
- ✚ Reduced supplier balances. Like sales, your costs are calculated based on what you purchased regardless of whether or not you have paid for the goods or services. If you owe less to your suppliers than you did at the start of the financial year then this means you have paid out more in cash than the expenses you've incurred since the start of the year.
- ✚ If you purchase assets the cost is capitalised and is not reflected in your profit.
- ✚ If you take money out of the business (drawings) this is not reflected in your profit calculation but does reduce the cash available to the business.
- ✚ Loan principal repayments. While interest costs are included when calculating your profit, the repayment of the loan principal isn't but it does actually cause a cash outflow.



Key reasons for cash to be higher than your profits

- ✚ Basically the main reasons cash may be higher than profit are the flip side of the above and include decreases in debtors and/or stock, increased creditors (payables), asset sales, new borrowings and cash introduced by owners.
- ✚ The other major difference is depreciation which is subtracted from profits but is not paid out in cash. Depreciation is essentially an allowance for the wearing out of assets used in the business.