

FOCUSING THE UCA CASH FLOW FORMAT ON LENDING OPPORTUNITIES

Various spread systems may be used to track cash flow. This article focuses on an adaptation of one such system—Uniform Credit Analysis®—to a format that the author calls “lender’s cash flow,” which helps bring more light to lending opportunities. This format is shown using a real-life example.

by James C. Miller

In 1987, RMA moved credit analysis from the horse-and-buggy days of traditional net-profit-plus-depreciation cash flow to the jet-age Uniform Credit Analysis® (UCA) format, a variant on the Financial Accounting Standards Board’s FASB95® cash flow format. The UCA format, which calculates real cash flow, is probably the best thing RMA has done for lenders since it started collecting and publishing comparable peer data.

However, over the years, experienced commercial lenders at large and small banks have told me that the UCA cash flow is ignored in certain situations. It is not required in some banks’ loan approval write-ups. It is not used by some vendor programs, such as LaserPro® (which produces loan documents), that use net profit plus depreciation in lieu of the UCA cash flow. Most important, though, it is not used by some lenders who, instead, go directly to companies’ financial statements to make “eyeball” estimates using net profit plus depreciation.

In my experience, such informal estimates work best when the situation is simple and obvious, and less well in complex and marginal situations. First, accurate cash-flow calculations can be too complex for most lenders to do off the top of their heads. Second, most financial statements show periods of only two years—not enough to establish the important trends and patterns. Third, the customers most likely to leave one bank for another tend to have

complex and often marginal financial situations, which require a more formal and detailed analysis. Indeed, they may be open to leaving their current banks because their current lenders calculate cash flow off the top of their heads, which may result in an opinion that is less accurate and less favorable than that of company management. I suggest that the limitations of the widely used informal “eyeballing” techniques are a disadvantage, because most commercial lenders face aggressive loan-growth goals and need a reasonably precise and easily used tool to help them identify lending opportunities quickly and avoid wasting time on candidates that ultimately end up being unsuitable.

Lenders’ Cash Flow

To solve that problem, I suggest a reorganization of the UCA/FASB95 format, which I’ll call *lenders’ cash flow* (LCF). LCF focuses on and directly displays precisely the lending opportunities for which experienced lenders look. This reorganization of the UCA format is not the first to be suggested¹, and it does not attempt to address subtle accounting or theoretical nuances for obscure kinds of companies. However, I believe it is the first to result in a simple, easily used format designed specifically to help commercial lenders in the real world focus quickly on lending opportunities.

What do experienced lenders look for? In general, lenders tell me they look for three things in the financial statement:

1. Some approximation of cash flow for debt repayment, to

find net profits and then mentally add back interest, taxes, depreciation, and amortization.

2. Lending opportunities in receivables and inventory,

because these assets are what the loan supports most of the time. They look at the magnitude and estimated change in these assets to get an idea of the size of any loans to cover the change. When you think about it, these elements constitute the asset part of the trading asset or working capital cash cycle.

3. Lending opportunities in capital expenditures by examining the size and changes in fixed assets, i.e., the asset portion of the capital expenditures cash cycle (CAPEX). These lenders know that financing fixed assets is a time-honored way to build large interest-income-generating outstandings quickly. Very savvy lenders have found that sometimes terming out high-equity fixed assets provides the cash to solve many business problems.

Figure 1

Current UCA Format	New "Lending Opportunities in Receivables & Inventory"	New "Lending Opportunities in CAPEX"	New "EBITDA/ NOI Interest Coverage"
Revenues			Revenues
Changes in Receivables	Changes in Receivables		
Cost of Goods Sold			COGS
Changes in Inventory	Changes in Inventory		
Changes in Trade Payables	Changes in Trade Payables		
Changes in Costs/Billings > Bills/Costs			
Other Operating Revenues & Non-Trade Receivables			
Operating Expenses			Operating Expenses
Changes in Operating Balance Sheet Items			
Cash Payments for Income Taxes			
Changes in Flooring Line			
Net Cash from Operations			
Cash CPLTD Payments (Current Portion of Long-term Debt)			
Cash Interest Payments			
Dividends			
Cash After Debt Amortization			
Non-Operating Income (Expense)			
Fixed Assets Changed		Fixed Assets Changed	
Cash Used for Investments			
Other Asset Transactions			
Changes in Intangibles			
Asset Sales/Extraordinary			
Changes in Short-term Bank Debt	Changes in Short-term Bank Debt		
Changes in Long-term Debt		Changes in Long-term Debt	
Changes in Subordinated Debt			
Changes in Other Liabilities and Affiliated Liabilities			
Changes in Other Liabilities & Gray Area			
Changes in Net Worth			
Net Change in Cash			
Beginning Cash			
Net Change in Cash			
Ending Cash			

Reorganizing UCA with Three New Focused Sections

Figures 1 and 2 show how I reorganized the UCA format to create three new sections that focus on and present what the lenders look for.

Interest coverage. For the interest repayment income stream, i.e., cash flow approximation, I chose interest, taxes, depreciation, and amortization (EBITDA) and accordingly moved revenues, cash cost of sales, and cash operating expenses to a section called New "EBITDA / NOI Interest Coverage." I chose EBITDA, sometimes referred to as *net operating income* (NOI), over the alternatives for four reasons:

1. It closely resembles the quick mental calculations experi-

Figure 2	
UCA	Proposed Lenders' Cash Flow (LCF)
Operating Cash Flow	Interest Coverage Lending Opportunities in Receivables & Inventory Miscellaneous Operating Cash Flow
Debt Coverage	Debt Coverage
Investing Cash Flow Financing Cash Flow	Lending Opportunities in CAPEX Remaining Sources & Uses

enced commercial lenders make and that, in actual practice, tend to be quickly accepted.

2. It has long been recognized that interest repayment comes from the profits earned on the sale of the assets funded by bank debt and that principal repayment comes from the liquidation of the funded asset. Well, EBITDA is the appropriate income stream that covers the interest portion.
3. There is widespread acceptance² of EBITDA in the general financial community, including commercial lenders and prospective customers, so bankers and borrowers usually speak the same language.
4. All the line items needed for calculation are already present in the existing UCA format.

Lending Opportunities in Receivables & Inventory. Next, I isolated the major elements that capture the trading asset cash cycle, i.e., changes in receivables and inventory, the changes in trade payables, and the short-term bank debt that funds those opportunities. I moved this cycle's elements from their location in the current UCA format to a new section, Lending Opportunities in Receivables & Inventory.

Lending Opportunities in

CAPEX. Finally, I isolated the major elements that capture the CAPEX cash cycle—i.e., the changes in fixed assets and the changes in the long-term debt that should fund most of the growth in fixed assets—and moved them to a new section, Lending Opportunities in Capital Expenditures (CAPEX).

Other Items. Remaining items in the Operating Cash Flow section of the UCA format include miscellaneous operating cash flow elements—mostly cash payments for income taxes. I grouped these line categories together in Miscellaneous Operating Cash Flow. In actual practice, moving these items out of Lending Opportunities in Receivables and Inventory allowed for clearer focus on the trading assets cash cycle. In addition, collecting these items in this new section made it easier to examine them and catch anomalous amounts that influenced cash flow.

I left intact the classic UCA Debt Coverage section, which includes the Cash After Operations (CAO) and the Cash After Debt Amortization (CADA) subtotals. This means the subtotals and debt coverage ratios are identical to those of the current UCA format.

I took the remaining miscella-

neous items and put them into the proposed LCD in a Remaining Sources and Uses section. In actual practice, this section proves very useful in tying up loose ends and answering some questions that arise from the other sections.

How It Works

Figures 3 and 4 show an example from real life. Figure 3 contains the income statement for the last year and the balance sheet for two periods, i.e., what is required to calculate cash flow. Figure 5 shows the cash flow derived from Figures 3 and 4 with the existing UCA format in the two columns to the left and the proposed Lenders' Cash Flow in the two columns to the right. Notice that the existing UCA format and the Lenders' Cash Flow use identical line items and identical Cash After Operations and Cash After Debt Amortization figures.

EBITDA / NOI Interest Coverage. Let's start at the top section in Figure 7, EBITDA / NOI Interest Coverage, the Lenders' Cash Flow format lets us look at the cash flow approximation section. In this case, the Lenders' Cash Flow presented the \$11.8 million in revenues and then subtracted \$6.994 million in cash costs of sales³ and \$3.970 million in cash operating expenses⁴. The result was EBITDA, or NOI, of \$846,000. This EBITDA covered \$284,000 in interest 2.9 times. My experience is that this is strong for any kind of company.

Normal EBITDA does not adjust for changes in receivables, but for some companies, this can be significant. As a result, the Lenders' Cash Flow also adjusts for changes in receivables to pres-

ent Cash EBITDA (which we could call CEBITDA). In this case, CEBITDA was a positive \$758,000 to cover the \$284,000 in interest for a coverage ratio of 2.6. The format makes both options available so the lender can choose which is more appropriate.

Lending Opportunities in Receivables & Inventory in the Operating Cash Cycle.

Figure 7 shows the lending opportunities in receivables and inventory in the “Lending Opportunities in Rec & Inv” section of the LCF. First we see changes in the two trading assets—the receivables and inventory—and then we see how those assets are funded by their normal sources of funds, which are increases in short-term bank lines of credit and trade payables. There is only a small lending opportunity to support receivables because they only increased \$88,000. However, there is a substantial lending opportunity in inventory, which increased \$1.3 million this year, certainly a portion of which experienced lenders would want to finance.

Next, note that trading assets (inventory and receivables) grew at a combined rate of 56.4%, as opposed to revenue at 28.2%. Because revenues and trading accounts should move at roughly the same rate, the faster growth in trading assets is a potential problem. On a dollar basis, the LCF shows that of the total \$88,000 growth in receivables, \$89,000 was required by the revenue growth⁵; however, only \$601,000 of the \$1.3 million of inventory growth was attributable to sales growth. The LCF will help us find what caused the portion of inventory growth not attributable to sales growth.

Now we need to look at the two funding sources—trade payables and short-term bank lines of credit. Trading accounts increased \$1.371 million, but only a tiny portion of that was covered by the \$85,000 increase in trade payable, leaving \$1.286 million to cover. The company borrowed a total of \$1.564 million in new advances on its short-term bank line of credit, but this was \$278,000 more than the \$1.286 million actually needed. Because we know the \$278,000 in advances on the line did not go into inventory or receivables, we’ll use the LCF to find out where it *may* have gone.

The possible misuse of the line of credit represents a potentially serious problem because it means availability on the line has now been reduced at precisely the time when the company needs increased availability to help support the increased revenue growth from the new national retail contracts. Incidentally, the Figure 7 section presents changes in trading assets in dollar amounts rather than in turndays. That’s because saying, for example, that you need to lend four more turndays is far less useful than saying you need to lend an additional \$350,000. In real life, we asked this customer about the increases in inventory and he told us he had landed contracts with two large retail chains for his kite

Figure 3

Income Statement		
(\$000s)	FY01	FY02
Revenues	9,210	11,810
Cost of Sales	5,449	6,994
Cost of Sales—Depreciation	156	153
Total Cost of Sales	5,605	7,147
Gross Profit	3,605	4,663
General & Admin Exp.	3,086	3,970
Interest Expense	205	294
Total Operating Expenses	3,291	4,264
Operating Profits	314	399
Interest Income	3	4
Other Income	36	79
Pretax Income	353	482
Federal Income Taxes	164	7
Net Profits	189	475

Figure 4

Balance Sheet		
Assets (\$000s)	FY01	FY02
Cash	9	3
Accounts Receivable	314	474
Less Bad Debt Reserve		72
Total Receivables	314	402
Total Inventory	2,119	3,402
Inventory Supplies	53	91
Total Current Assets	2,495	3,898
Total Fixed Assets	381	1,028
NonOpL/T Invest in Sub	30	15
Prepaid Oth (Op) & Deposits	161	284
Deffered Inc. Tax Recoverables	15	
Total Noncurrent Assets	206	299
Total Assets	3,082	5,225
Liabilites	FY01	FY02
Credit Line—Banks	822	2,386
Current Port. LT Debt—2	81	65
Current Port. LT Debt—Capital Lease		18
Trade Accounts Payable	1,043	1,128
Other Accruals	236	257
Income Taxes Payable	71	
Loans From Related Parties		90
Total Current Liabilites	2,253	3,944
Long-term Debt—2	104	44
Long-term Debt—Capital Lease		53
Total Noncurrent Debt	104	97
Total Debt	2,357	4,041
Commom Stock	9	9
Retained Earnings	716	1,175
Total Equity	725	1,184
Total Debt + Equity	3,082	5,225

products and built up inventory in the third quarter to start deliveries for the Christmas season. Consequently, we can defensibly conclude that the growth in inventory was “good” and probably represented a legitimate lending opportunity. However, the company still borrowed more than it needed and we need to find out why.

Advances on short-term lines of credit other than flooring lines or notes payable real estate are generally not considered part of net cash after operations or net cash after debt amortization.⁶ Consequently, the section contains an adjustment line to remove the \$1.564 million in changes in short-term bank debt from the calculations. This will also allow the LCF to match the UCA’s CAO and CADA subtotals.

Miscellaneous Cash Flow.

Miscellaneous cash flow for most companies is cash payments for income taxes plus other minor, immaterial, and incidental cash inflows and outflows, the latter of which are seldom significant. That’s why, if they *are* material, you should examine them to find their cause and see if they harm the company. As it turns out, this example shows \$63,000 paid in cash for income taxes, but it also shows an anomaly—a \$140,000 cash outflow. When asked, the customer said he’d borrowed this from the company for personal uses (and *not* for payment of personal taxes) before he landed the contracts with the retail chains.

A defensible conclusion is that the owner’s draw may not have harmed the company when it was made before the contracts were signed, but now that cash is

needed to support sales driven higher by the contracts, the absence of the cash is harmful.

But it also represents an opportunity for the lender to figure out a way to lend reinjects the cash

Figure 5

Current UCA Format		Proposed Format	
		EBITDA / NOI Interest Coverage	
Revenues	11,810	Revenues	11,810
Changes in Receivables	(88)	Cash Cost of Sales	(6,994)
COGS	(6,994)	% of Revenues	-59.2%
Changes in Inventory	(1,283)	Cash Operating Expenses	(3,970)
Changes in Trade Payables	85	% of Revenues	-33.6%
Changes in Costs/Billings > Bill Costs		EBITDA (NOI)	846
Other Operating Rev & Non-Trade Rec			7.2%
Operating Expenses	(3,970)	Interest Cash Payments	284
Changes in Op. Balance Sheet Items	(140)	EBITDA / Cash Interest Expense	2.9
Cash Payments for Income Taxes	63	CEBITDA (Adj for Rec)	758.0
Changes in Flooring Line	0	% of Revenues	6.4%
		EBITDA / Cash Interest Expense	2.6
		Cash Flow from EBITDA	\$846
		Lending Opportunities in Receivables & Inventory	
		Receivables (Increase) Decrease	(88)
		Inventory (Increase) Decrease	(1,283)
		Cash Absorbed into Trade Assets	(1,371)
		Revenue Growth Rate	28.2%
		Trading Account Growth Rate	56.4%
		Receivables Change Due to Rev Growth	(89)
		Inventory Change Due to CCOG Growth	(601)
		Trade Payables Increase (Decrease)	85
		Short-term Bank Debt Increase (Decrease)	1,564
		Financing Provided	1,649
		Financing Surplus (GAP)	278
		Adjust Short-term Bank Debt	(1,564)
		UCA Financing Surplus (GAP)	(1,286)
		Miscellaneous Cash Flow	
		Changes in Costs/Billings > Bill/Costs	0
		Other Op Rev & Non-Trade Rec	0
		Changes in Op Balance Sheet Items	
		Cash Payments for Income Taxes	(63)
		Miscellaneous Cash Sources (Uses)	(203)
Cash Flow (Net Cash From Operations)	(643)	Net Cash Flow After Operations	

Figure 5 continues on the following page

back into the company if suitable collateral and repayment can be found. As it turns out, this suggested Lenders' Cash Flow gives us the tools to do just that.

Cash-Based Debt Coverage.

Positive Net Cash Flow After Operations of a negative \$643,000—less principal, interest payments, and dividends—gives

us Net Cash After Debt Amortization, which is identical to the same subtotal in the UCA format. If we use Net Cash Flow After Operations as a numerator and the total of the items covered as the denominator, we get a negative (1.7) debt coverage ratio (DCR). On the surface, negative DCRs always look bad, but remember that this specific nega-

tive DCR was caused by production for the new contracts.

Before we go any further, we need to adjust back the changes in short-term bank debt, which we had previously removed to match the UCA's CAO and CADA. This gives us cash flow before capital expenditures (CAPEX) of a positive \$546,000.

CAPEX Cash Cycle.

The third thing the current UCA format does not display (after interest coverage and lending opportunities in receivables and inventory), but which experienced lenders want to see is the lending opportunities in CAPEX. Lending opportunities in CAPEX are second in importance only to the opportunities in receivables and inventory. Not only does the CAPEX cycle represent a major source of lending opportunities and problem-solving for bankers, but it also gives insight into the financial sophistication of the borrower. Borrowers with financial sophistication know they should match the life of the asset with the maturity of the funding; in this case, you should purchase long-term fixed assets largely with long-term debt rather than with cash. Lenders with financial sophistication know high-equity fixed assets present opportunities for lenders to help the customer restructure debt and get out of trouble. All other things being equal, the financing of fixed assets at roughly 65% to 85% of value, depending on your bank's policy for such construction or term loans, can represent a lending opportunity to finance the purchase of fixed assets, to term out fixed assets erroneously purchased with cash by financially unsophisticated management, and as a source of

Figure 5 (continued)

Current UCA Format		Proposed Format	
		Cash-based Debt Coverage	
Cash CPLTD Payments	(81)	Cash CPLTD Payments	(81)
Cash Interest Payments	(294)	Cash Interest Payments	(294)
Dividends	0	Dividends	0
Cash After Debt Amortization	(1,018)	Net Cash After Debt Amortization	(1,018)
Non-Operating Income (Expense)	83	Cash-based Debt Coverage	(1.7)
Cash Fixed Additions	(800)	<i>Adjusted Used Short-term Bank Debt</i>	1,564
Cash Used For Investments	15	Net Cash Flow Before CAPEX	546
Other Asset Transactions		Lending Opportunities CAPEX	
Changes in Intangibles		Year-End Fixed Asset Equity	931
Asset Sales/Extraordinary		CAPEX (Increase) Decrease	(800)
Changes in Short-term Bank Debt	1,564	L/T Debt Increase (Decrease)	76
Changes in Long-term Debt	76	CAPEX Financing Surplus (GAP)	(724)
Changes in Subordinated Debt		Cash After CAPEX	(178)
Changes in Other Liabilities & Affiliated Liabilities	90	Remaining Sources and Uses Section	
Changes in Other Liabilities & Gray Area		Sources	
Changes in Net Worth	(16)	Cash After CAPEX	
Net Change in Cash	(6)	Other and Accrued	188
Beginning Cash	9	Net Worth Increased	0
Net Change in Cash	0	Cash Account Decreased	6
Net Change in Cash	(6)	Total Sources	194
Ending Cash	3	Uses	
Actual Cash Flow Coverage	(1.7)	Cash Flow Shortfall After CAPEX	(178)
		Other and Accrued	0
		Net Worth Reduced	(16)
		Total Uses	(194)

Figure 6			
(\$000s)	Sources	Uses	
EBITDA	\$846	(\$203)	Miscellaneous Cash Flow
Inventory Financing Surplus	\$278	(\$294)	Interest
		(\$81)	CPLTD
Total Sources	\$1,124	(\$578)	Total Uses
Net Surplus	\$546		

secured long-term financing to ease a customer's cash flow tightness.

In this specific case, the \$76,000 increase in long-term debt was only 9.4% of the \$800,000 increase in fixed assets and left a financing gap of \$724,000. To see what could have covered this, consider that we already have a positive surplus before CAPEX of \$546,000, left over from the positive EBITDA and the positive surplus of financing (including advances on the line, which were not needed) over investment in real estate. This will cover most of the CAPEX, to leave us a CAPEX financing gap of \$176,000. And we're about to find sources to cover that in the Remaining Sources and Uses section.

Remaining Sources and Uses. This shows sources of funds of \$6,000 by drawing down existing cash and \$188,000 in Other and Accrued for \$194,000. This is more than enough to cover the shortfall of \$178,000 from CAPEX. The \$188,000 unravels—through questions to the owner—to consist of several insignificant transactions and a couple of material ones. One material transaction totals \$175,000, consisting of:

- \$79,000 in Other Income earned annually by renting out unused office space at the manufacturing facilities; thus,

it is a genuine cash source.

- Also genuine, although not recurring, is a net \$90,000 in loans from the owner to the company.
- A \$6,000 reduction in cash.

The \$175,000 is, for all practical purposes (considering that we're dealing with rounded-off numbers), the rest of the remaining shortfall. That means the fixed asset purchases ended up being covered by the surplus of cash flow plus some miscellaneous sources, including cash back from the owner, which, in turn, means it is possible that the fixed assets were partly funded by the unneeded advances on the line of credit.

In the real world, the actual chronology can vary from what we calculated here. The purchase of the fixed assets may have come first, leaving the company with a cash flow shortfall that the owner had to ante up for later (or get line advances); thus, the linkage between loan, line of credit, and fixed assets may not have been clear to the owner at the time. Rather, the line advances may have appeared to be simply a requirement to make payroll or to cover some other expense.

Several final words on this section. At this point in the cash flow report, the sources always exactly equal the uses. In addition, this section often turns out to be

very useful in identifying drains out of the company that deserve scrutiny and in answering questions that arise as the banker goes down the format. Finally, the LCF does not present a balance-to-cash display, as does the current UCA, but it uses cash just like any other asset that is increased or decreased. There's nothing magic about balancing to cash other than to persuade lenders that the report "balances." Indeed, mathematically, the report's last line could balance to any category. It's more important to know where cash came from or what it was or will be used for. The sources and uses presentation allows lenders to look for answers to those questions.

What Has the New LCF Told Us?

The new suggested format has told us several things the current UCA format does not.

1. It tells us that this company has at least adequate core cash flow for interest repayment.
2. It displays significant lending opportunities in trade accounts, particularly as sales take off because of the new national contracts.
3. It displays a significant lending opportunity in CAPEX, which has adequate equity (\$1.028 million in fixed assets supported by \$97,000 in long-term debt, leaving equity of \$931,000) to be termed out. Among other things, this equity could support long-term debt to help support inventory growth to fuel sales and it might even be used to help inject cash back to replace what the owner borrowed.
4. It also tells us that some of the surplus advances on the

Figure 7

Lenders' Cash Flow	
EBITDA / NOI Interest Coverage	
Net Profit	475
Plus Depreciation & Amortization	153
Traditional Cash Flow	628
Plus Interest, Taxes & Other Income, Other Expenses	218
Earnings Before Interest, Taxes, Depreciation & Amortization	846
Revenues	11,810
Cash Cost of Sales	(6,994)
% of Revenues	-59.2%
Cash Operating Expenses	(3,970)
% of Revenues	-33.6%
EBITDA	846
% of Revenues	7.2%
EBITDA/Interest Expenses	2.9
CEBITDA	758
% of Revenues	6.4%
CEBITDA/Interest Expense	2.6
Lending Opportunities in Receivables & Inventory	
Receivables (Increase) Decrease	(88)
Inventory (Increase) Decrease	(1,283)
Cash Absorbed into Trade Assets	(1,371)
Revenue Growth Rate	28.2%
Trading Account Growth Rate	56.4%
Receivables Change Due to Revenue Growth	(89)
Inventory Change Due to Revenue Growth	(601)
Trade Payables Increase (Decrease)	85
Short-term Bank Debt Increase (Decrease)	1,564
Financing Provided	1,649
Financing Surplus (GAP)	278

line of credit may either have helped to cover advances to the owner, or, along with strong EBITDA, to cover the fixed assets—in either case, a possible misuse of short-term bank debt. However, the inappropriate use of cash flow or line advances to purchase fixed assets gives the banker the opportunity to add value to the relationship and earn

Figure 7 (continued)

Lenders' Cash Flow	
Adjusted Short-term Bank Debt	(1,564)
UCA Financing Surplus (Gap)	(1,286)
Miscellaneous Cash Flow	
Changes in Op. Balance Sheet Items	(140)
Cash Payments for Income Taxes	(63)
Miscellaneous Cash Sources (Uses)	(203)
Net Cash Flow After Ops	(643)
Cash-Based Debt Coverage	
Cash CPLTD Payments	(81)
Cash Interest Payments	(294)
Dividends	0
Net Cash After Debt Amortization	(1,018)
Cash-based Debt Coverage	(1.7)
Adjust Already Used ST Bank Debt	1,564
Adjust Net Cash Flow After Amortization	546
Lending Opportunities in Fixed Assets	
Year-End Fixed Asset Equity	931
CAPEX (Increase) Decrease	(800)
L/T Debt Increase (Decrease)	76
CAPEX Financing Surplus (Gap)	(724)
Cash After CAPEX	(178)
Remaining Sources and Uses	
Sources	
Other and Accrued	188
Cash Account Decreased	6
Total Sources	194
Uses	
Cash Flow Shortfall After CAPEX	(178)
Net Worth Reduced	(16)
Cash Account Increased	
Total Uses	(194)

additional interest and fees by terming out the equity in the fixed assets.

Not Just for Lending Opportunities

Use of the Lender's Cash Flow not only helps identify lending opportunities, it also helps write more meaningful credit analyses because it presents the specific cause-and-effect relationships for the two different cash

cycles and the repayment stream. Having the logic already visible and obvious makes it easier to put into writing. □

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Notes

1 For example, see Cassis, John, "Cash Flow or EBITDA? Can't We Have Both?" *The RMA Journal*, December 2002, pp. 26-34, which reorganizes the UCA format into the "Matched-Allocation Performance Statement."

2 It is true that EBITDA has its supporters and detractors, and there are valid arguments for and against published in other financial publications as well as *The RMA Journal*. For example, see Cassis, *ibid.*, and also see Strischek, Dev, "E-B-I-T-D-A: It Doesn't Spell 'Cash Flow,'" *The RMA Journal*, November 2001, pp. 30-40, the latter with excellent references to both sides of the argument. But perhaps the partisans will condone the use of EBITDA limited to interest coverage only.

3 Cost of goods sold (or cost of sales) less any noncash items, such as depreciation, amortization, capitalized interest, etc.

4 Cash operating expenses less any noncash items, such as depreciation, amortization, allowance for bad debts, etc.

5 There are several ways to calculate the impact of growth on the changes in receivables and inventory. For this example, I used the following formula to estimate the impact on growth on the changes in receivables: $((PP \text{ NetRec} / PP \text{ Sales}) \times CP \text{ Sales}) - PP \text{ NetRec}$. PP means *prior period*, CP means *current period* and NetRec means *receivables less such noncash items as a bad debt reserve*. And I used the following formula for the changes in inventory: $((PP \text{ Inv} / PP \text{ Cash COGS}) \times CP \text{ Cash COGS}) - PP \text{ Inv}$. In this case, Cash COGS means *cost of goods sold (or cost of sales)*, less any capitalized items or noncash items, such as depreciation.

6 The exceptions are car dealers, real estate developers, and other companies using flooring-type, or asset-based, debt to finance the inventory. For these entities, advances on the line of credit are appropriately counted as part of cash flow, and no adjustment is made to remove them from the calculations.