Cash Flow vs. Fund Flow

There are generally four different kinds of financial statements in accounting: the balance sheet, the income statement, the cash flow statement, and the fund flow statement. Here, we delve into the final two.

In financial accounting, the statement of cash flows refers to the change in a company's cash and equivalents from one period to the next. The fund flow, however, has two different meanings. One is for accounting purposes, while the other serves investment purposes.

Cash Flow

Cash flow is recorded on a company's cash flow statement. This statement—one of the main statements for a company—shows the inflow and outflow of actual cash (or cash-like assets) from its operational activities. It is a required report under generally accepted accounting principles (GAAP).

This is different from the income statement, which records data or transactions that may not have been fully realized, such as uncollected revenue or unpaid income. The cash flow statement, on the other hand, will already have this information entered and will give a more accurate portrait of how much cash a company is generating.

Cash flow sources can be divided into three different categories on a cash flow statement:

- Cash flows from operating activities: Cash generated from the general or core operation of the business would be listed in this category.
- Cash flows from investing activities: This section would cover any cash flow spent on investments like new equipment.
- Cash flows from financing activities: This category includes any transactions involving debtors, such as proceeds from new debts or dividends paid to investors.

Companies receive inflows of cash revenue from selling goods, providing services, selling assets, earning interest on investments, rent, taking out loans, or issuing new shares. Cash outflows can result from making purchases, paying back loans, expanding operations, paying salaries, or distributing dividends.

Since the Securities and Exchange Commission (SEC) requires all listed companies to use accrual accounting, which largely ignores the actual balance of cash on hand, investors and lenders rely on the statement of cash flow to evaluate a company's liquidity and cash flow management. It is a more reliable tool than the metrics companies use to dress up their earnings, such as earnings before interest, taxes, depreciation, and amortization (EBITDA).

Fund Flow

In the accounting side, the fund flow statement was required by GAAP between 1971 and 1987. When it was required, the statement of fund flow was primarily used by accountants to report any change in a company's net working capital, or the difference between assets and liabilities, during a set period of time. Much of this information is now captured in the statement of cash flow.

[Important: For investment purposes, the fund flow does not give the cash position of a company; if a company wanted to do that, it would prepare its cash flow statement.]

The fund flow highlights the movement of cash only—that is, it reflects the net movement after examining inflows and outflows of monetary funds. It will also identify any activity that might be out of character for the company, such as an irregular expense.

The use of the fund flow statement in investing is more useful today. Investor sentiment can be gauged as it relates to different asset classes. For example, if the flow of funds for equities is positive, it suggests investors have a generally optimistic view of the economy—or at least the short-term profitability of listed companies.

Key Takeaways

- *A company's cash flow and fund flow statements reflect two different variables during a specific period of time.*
- *The cash flow will record a company's inflow and outflow of actual cash (cash and cash equivalents).*
- *The fund flow records the movement of cash in and out of the company.*
- *Both help provide investors and the market with a snapshot of how the company is doing on a periodic basis.*