Financial Modeling, Cash Flow Projections and Liquidity Management

**Issue**

As companies are increasingly likely to encounter financial distress due to a myriad of economic and industry-specific reasons, it is critical to forecast future liquidity needs and operational performance accurately. A precise but flexible financial forecasting model is essential to project cash flows of the business properly, which ultimately govern viability. Without sufficient liquidity, there is no business.

Companies facing a sustained or sharp decline in profitability, decreasing revenues or constrained liquidity are often in need of corporate restructuring, turnaround or insolvency-related services, depending on the specifics of the business and its unique circumstances and challenges.

In order to assess the viability of various options and determine the appropriate strategy for turnaround or reorganization, management must be able to forecast various profitability and liquidity scenarios reasonably. It is therefore paramount to have a flexible integrated three-statement projection model that can be modified quickly to accommodate varying assumptions for key business and liquidity drivers.

**Challenges and Opportunities**

Although management often understands the key business drivers of the company’s operations and cash position, modeling and quantifying the specific impact of changes to such drivers is no easy undertaking for an already busy management team.

To complicate matters, when dynamic business changes are taking place – as is often common in restructuring, turnaround and insolvency situations – the task of accurately projecting the impact of those changes on the profitability and liquidity of a business becomes increasingly complex and difficult to perform accurately and efficiently. Key challenges include:

- **Lack of available personnel.** Often when the need arises to create a dynamic integrated projection model to examine strategic alternatives, the company is already facing resource constraints. Managing the day-to-day issues associated with such liquidity crises requires significant attention of management and staff, and existing personnel often do not have the capacity to undertake new projects.

- **Insufficient experience or qualifications and quality and accuracy of results.** If current personnel have the bandwidth to dedicate to the development of a dynamic projection model, the experience or qualifications required to develop a flexible model that can accurately forecast liquidity and operational performance under a given set of inputs or assumptions may not exist.

- **Timing and efficiency.** Due to the time-sensitive nature of obtaining results and making decisions when a company is in financial distress, efficiency and execution in a timely fashion are critical but often difficult to achieve.

**Our Point of View**

Companies undergoing financial distress should analyze historical financials, understand key business drivers, assess the current industry and economic environment, and develop a flexible financial model that can easily be adjusted. When liquidity is especially tight, they should develop weekly (or even daily) cash flow projections to monitor and manage cash flow closely.

Under these circumstances, many organizations choose to bring in corporate restructuring experts for guidance and assistance.
How We Help Companies Succeed

Because a company’s best strategic alternative is sometimes a bankruptcy filing, our restructuring professionals can prepare required 13-week cash flow projections under both cash collateral and DIP financing scenarios to ensure liquidity will be available as the company uses the bankruptcy process to restructure.

Our team can quickly develop an integrated three-statement financial projection model that will forecast income statements, balance sheets, and statements of cash flows for the coming weeks, months and years.

Working with management to identify key business drivers and major assumptions, we incorporate a flexible “dashboard” within the projection model where those inputs can easily be changed to run base-case, upside and downside scenarios. A flexible cash flow model is critical for sensitizing certain business decisions, such as whether to divest certain assets, shut down a manufacturing facility, defer capital spending, close marginally performing locations or seek alternate financing.

Examples

National Hardware Retailer
Protiviti assisted a $4 billion retailer facing financial difficulty in developing a flexible integrated three-statement projection model that forecasted operations and liquidity over the upcoming five years. Prior to our involvement, the company was facing constrained liquidity and maturing debt combined with significant accounting restatements. Protiviti’s projection model was used by the company to assess liquidity needs and appropriately size both a revolving line of credit and bond issuance, and was also used by the lead agent for raising subscriptions to the lending syndicate. With our assistance, the company successfully raised $300 million in a revolving line of credit and an additional $300 million in bond debt (both of which were oversubscribed) to ensure sufficient liquidity during even the worst possible downside scenarios. Our client avoided what initially appeared to be an imminent bankruptcy filing.

National Direct Mail Printer
Protiviti helped a national printer identify strategic alternatives in light of declining revenue, deteriorating profitability and a liquidity crisis. Protiviti identified areas to reduce expenses, shed idle assets and improve profitability, while simultaneously developing an integrated projection model with a short-term cash flow forecast to support obtaining replacement financing. We contacted and negotiated with several potential lenders and ultimately assisted the company with obtaining amendments and maturity extensions of its secured debt and additional financing to avoid a shutdown of operations. As the company was a victim of a shrinking industry and faced significant union-related labor burdens, we ultimately guided the company into bankruptcy and prepared several 13-week cash flow projections and closely monitored collateral and cash positions. We led a successful sale process of the business, resulting in value maximization for all parties, full repayment of the secured lender, and redeployment of the physical assets.

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About Protiviti

Protiviti (www.protiviti.com) is a global consulting firm that helps companies solve problems in finance, technology, operations, governance, risk and internal audit. Through our network of more than 70 offices in over 20 countries, we have served more than 35 percent of FORTUNE 1000® and FORTUNE Global 500® companies. We also work with smaller, growing companies, including those looking to go public, as well as with government agencies.

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