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EXPRESS DIAGNOSTICS OF FINANCIAL STATE OF THE ENTERPRISE MEANS LIQUID CASH FLOW

One of the signs that allows to classify cash flows of the enterprise is an opportunity to ensure the solvency of the company. There are two types of cash flow that can be defined according to this sign: liquid and illiquid.

Liquid cash flow is one of the indicators which characterizes the financial stability of the company. It shows the changes in net credit position of the company within a certain period. Net credit position – is the difference between the sum of credits received by firms and magnitude of money [1, p. 119].

Zagorodniy A. gives the following definition of liquid cash flow – the cash flow, for which the ratio of supplementary (incoming) (Fi) and negative (output) (Fo) flows for a certain time is not less than one, that means that the conditions are met ($\frac{F_i}{F_o} \geq 1$) and illiquid – cash flow for which the ratio of supplementary (incoming) (Fi) and negative (output) (Fo) flows for a certain time is less than one, that means that conditions are observed ($\frac{F_i}{F_o} < 1$) [2, p. 703].

Liquid cash flow is closely related to the indicator of financial leverage (lever), which shows the extent to which the activities of the enterprise may be improved by bank credits.

The effect of financial leverage (DFL) is calculated using the formula:

$$DFL = (1 - TRP) \cdot (ROA - \overline{C}_A) \cdot \frac{LC}{EC}, \tag{1}$$

where TRP – Tax Rate Profit, the proportion of units;

   R_{OA} – return on assets, %

   $\overline{C}_A$ – the calculated average interest rate on the credit, %;

   LC – Loan Capital;

   EC – Equity Capital;

   $\frac{LC}{EC}$ – debt ratio (financial dependence).

By a positive DFL meaning, return on equity increases (provided that ROA > $\overline{C}_A$). By a negative DFL value, return on equity decreases, this means that a credit received by the company was not used appropriately.

Financial leverage can be regarded as an objective factor that arises with the appearance of borrowed funds in the company and provides an additional net income to equity.

It should be noted that the liquid cash flow is an indicator of deficient or excessive cash balances of the company if it fully covers all debt obligations. The formula for calculating liquid cash flow is as follows:

$$LCF = (LTC_e + CC_e - C_e) - (LTC_b + CC_b - C_b), \qquad (2)$$

where:

LCF – liquid cash flow;
LTC_e – Long Term Credits at the end of period;
CC_e – Current Credits at the end of period;
C_e – Cash at the end of period;
LTC_b – Long Term Credits at beginning of the period;
CC_b – Current Credits at beginning of the period;
C_b – Cash at beginning of the period.

The difference between the rate of liquid cash flow from other liquidity markers (absolute, fast, current) is that the latter characterize the company's ability to repay its liabilities, so they are more important for outside stakeholders (creditors). And liquid cash flow characterizes the absolute value of cash received from the ordinary activities of the enterprise and therefore is more "internal", closely related to the efficiency of operation of the business, it is important for its managers and owners, as well as potential investors. This indicator shows the impact of loans and credits on the effectiveness of enterprise's activity and ensures its financial flexibility. Liquid cash flow can be used for express diagnostics of the financial condition of the enterprise. Calculation of liquid cash flow can be made by the indexes of the cash flows and by the balance of funds in the accounts.

Unfortunately, the liquid cash flow has not become a widespread practice for rapid diagnosis at enterprises, but it is used by some banks in their work to determine the creditworthiness of customers, because it may help to define solvency.

References:
1. Bocharov V., Finansoviy analiz. Kratkiy kurs, 2-izd, SPb. Piter, 2008, p. 240.
2. Finansovo-ekonomichniy slovnik, uklad. Zagorodniy A., Voznyuk G. Kyiv, Znannya, 2007, p. 1072.