



CASH FLOW IS KING

The Art of Detecting 'Paper Profits' Before They Collapse





Profit is an Opinion. Cash is a Fact.

Why the 'Scoreboard' often lies about the game

THE AMATEUR VIEW (Scoreboard)

- Revenue Growth
- Net Profit
- EPS

NET PROFIT (PAT)

THE PRO VIEW (Reality)

- Operating Cash Flow

OPERATING CASH FLOW (OCF)

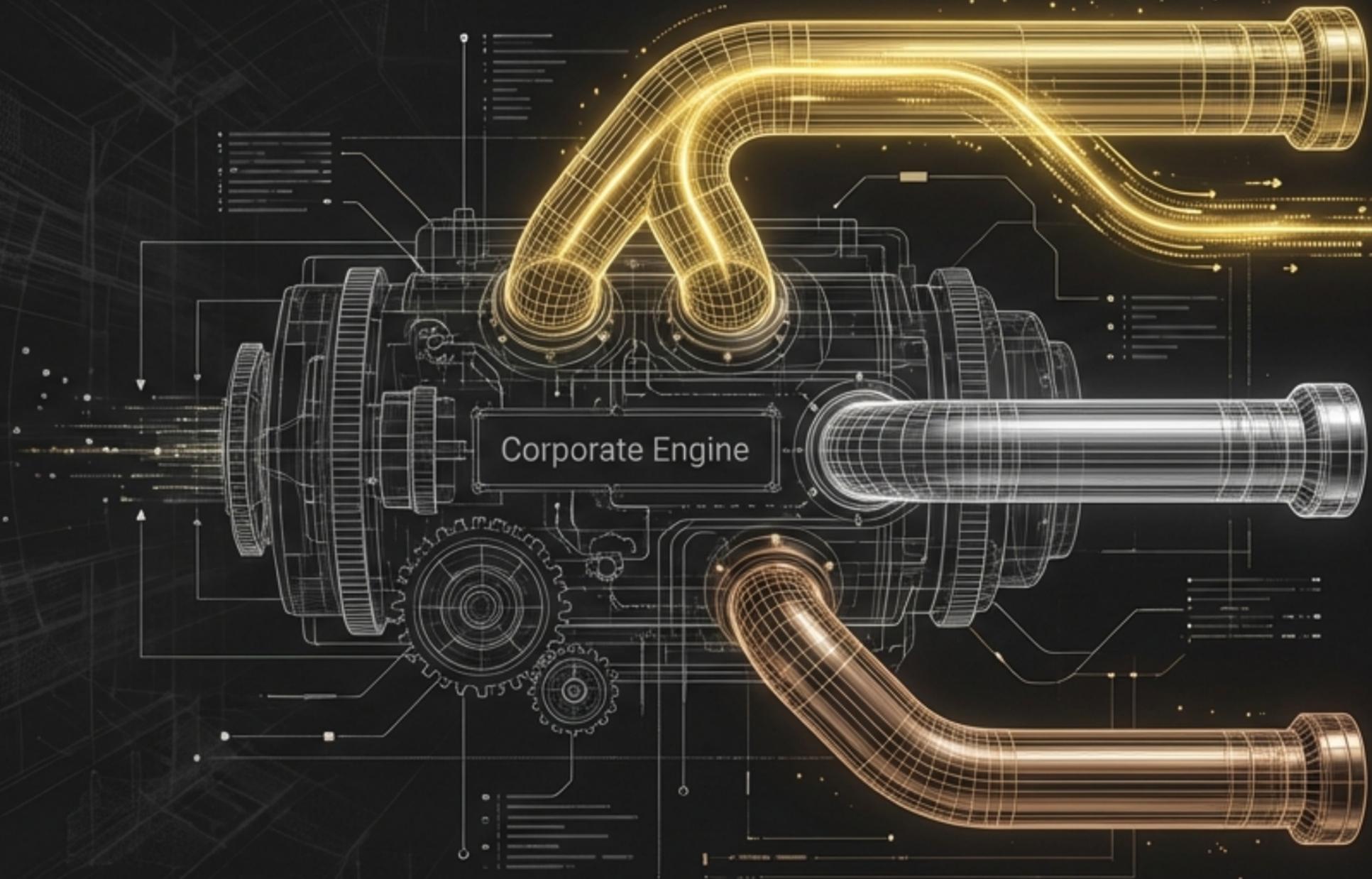
Insight:

Profit is recorded when a bill is raised (Accrual).
Cash is recorded when money hits the bank (**Reality**).



The Three Engines of Survival

Anatomy of the Cash Flow Statement



1. OPERATING CASH FLOW (OCF)

The Heartbeat. Cash from core business sales. The only sustainable fuel.

FORENSIC RULE: CRITICAL CHECK

Is the business generating its own fuel, or **burning furniture** to stay warm?

2. INVESTING CASH FLOW (ICF)

Asset Growth. Cash used for Capex or from selling assets.

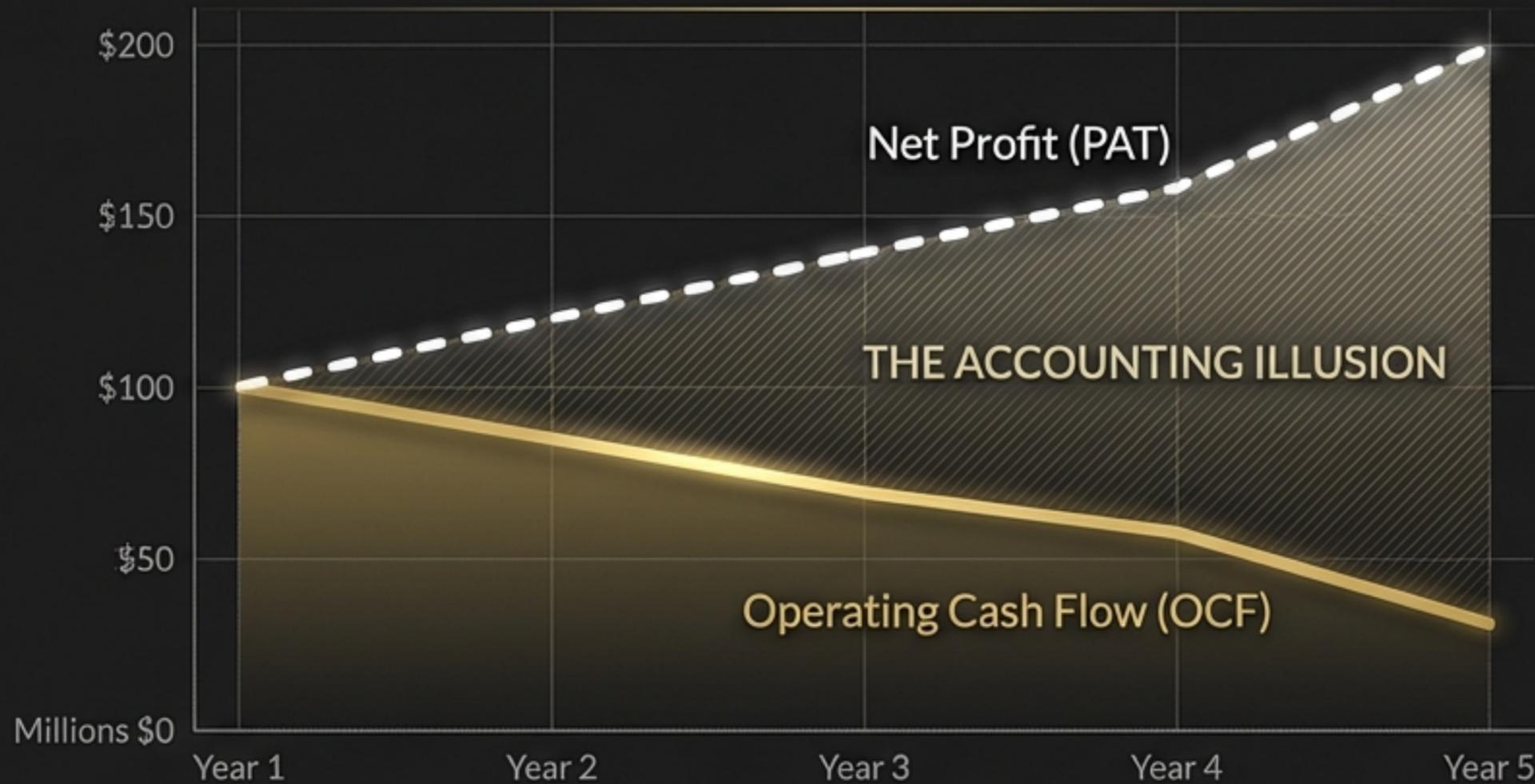
3. FINANCING CASH FLOW (FCF)

Life Support. Cash from loans or equity.



Diagnosing the 'Paper Profit' Trap

Divergence Chart



The 4 Red Flags

1. High Receivables (Stuffing channels)
Sales recorded, cash uncollected.
2. Inventory Build-up (Goods piling up)
Unsold goods inflate assets.
3. Aggressive Revenue Recognition
Booking future sales now.
4. Capitalized Expenses
Treating costs as assets.

FinReason Insight

Insight: If Profit goes **UP** but Cash Flow goes **DOWN**, the business is hollow.



The Litmus Test: Cash Conversion Ratio

$$\text{Cash Conversion Ratio} = \frac{\text{Operating Cash Flow}}{\text{Net Profit}}$$



CASH MACHINE
Collecting cash faster than paying bills.



WEAK
Profit stuck in receivables/inventory.



CRITICAL
Bleeding cash despite profit.

Real World Calculation



Reported Profit: ₹100 Cr



Operating Cash Flow: ₹40 Cr



Ratio: 0.4



Only 40% of profit is real. High Risk.



Forensic Analysis in Action: Yashtej Industries

The Surface Story

- Revenue Exploded (20x)
 - Loss turned to Profit (₹11.57 Cr)
- ₹12 Cr to ₹324 Cr
(20x Jump)



The Forensic Questions

- Did OCF match the 20x jump?
- Is Debt funding the inventory?
- Is Working Capital under strain?

Insight

Insight: Extreme disparity between Reported Growth and Cash Flow demands immediate forensic scrutiny.



The 'Growth Death' Spiral

How the Working Capital Trap kills growing companies.





‘Dressing the Bride’: IPO Red Flags

Manipulations to watch before listing.

- ▶ **Negative Operating Cash Flow**
(Despite rising profit)
- ▶ **Sudden Jump in Receivables**
(Booking future sales now)
- ▶ **Other Income Boosting PAT**
(Selling assets)
- ▶ **Capex Funded by Debt**
(Not internal accruals)



IPO money temporarily fixes ratios, but rarely fixes the business model.

Why Markets Punish the Illusion



- Valuation is the **Present Value** of **Future CASH FLOWS**, not Future **Accounting Profits**.
- When the market detects weak **cash flow** + **rising debt**, the correction is 50-70%.

The FinReason 5-Step Cash Flow Checklist™



TREND CHECK: Do PAT and OCF move together over 3-5 years?



RATIO CHECK: Is Cash Conversion Ratio > 0.7 ?



EFFICIENCY CHECK: Are Debtor Days stable?



SOURCE CHECK: Is debt rising to fund operations?



STRESS TEST: What happens to liquidity if revenue drops 20%?

Separating Speculative Earnings from **Durable Businesses**.



Think Like an Owner, Not a Trader

Revenue creates Excitement.

Profit creates Headlines.

Cash creates SURVIVAL.



In Investing: Cash Flow is King.



Disclaimer



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