The Value of Considering Cash Flow Risk and Total Cash Required

As you can see from the spreadsheets you developed in the prior lesson, a number of properties that meet the $6,000 profitability cutoff do not become cash-flow positive until some time in the year after the first conversion year. Sum the two years to identify any properties that are still net cash flow negative after two years.

If there are any such properties, it might be prudent to exclude them from an initial investment in the new business model, even though they are expected to be profitable.

It is also worthwhile to consider how much cash would be required for Capital Expenditures to do conversions for all the properties above the profitability cutoff. If Watershed is a small company, it may not have enough cash on hand to fund this; therefore, it would need to borrow some or all of the money in order to fund the conversions of all of the properties. There is always some risk associated with borrowing – if, through unforeseen problems, a company is unable to pay contractually required interest on its debt, it can even be forced into involuntary bankruptcy. The quicker the pay-back period on any loan, the better. So it is worthwhile to check the profitable properties to determine if any are still cash-flow negative after two years.