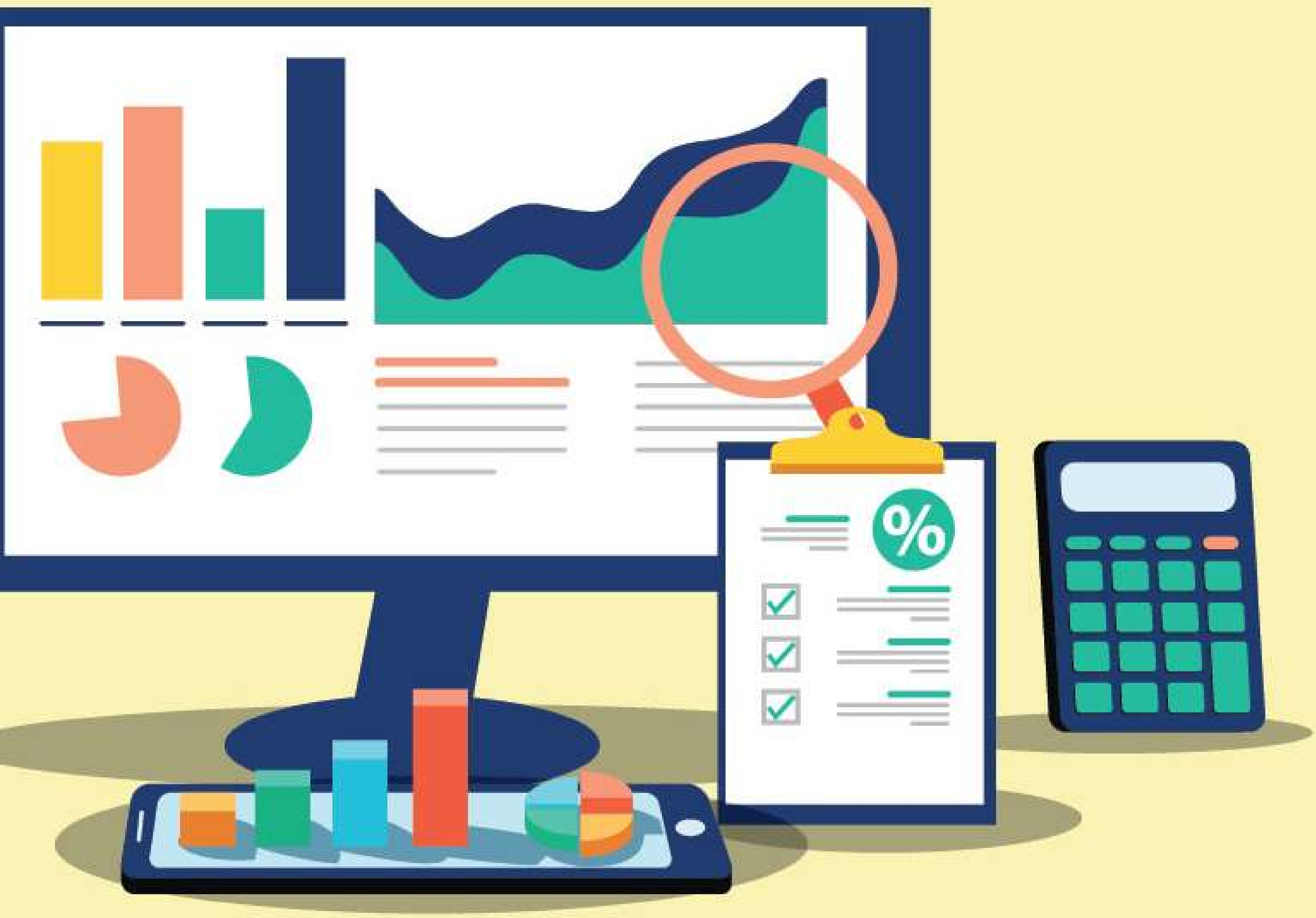
CASH FLOW

A Guide To Cash Flow



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OUR GUIDE TO IMPROVE YOUR CASH FLOW CASH FLOW IS KEY

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£25,000 equates to 37 months of average mortgage payments.

“Key to government modern industrial strategy is to address this issue”.

£25,000 equates to 9 average family holidays.

Small business minister Kelly Tolhurst says this is key to the UK economy.

In the UK alone 50,000 SME business fail annually due to cash flow issues.

The average outstanding cash owed beyond terms is circa £25,000. £25,000 is 11 months of the average salary.

5.7 million small businesses are the backbone of the UK economy.

THE DEFINITION OF CASH FLOW MANAGEMENT IS;

The process of monitoring, analysing and optimising the net amount of cash receipts minus cash expenses.

Net CASH FLOW is a key measurement of the financial health of a business.

Until there is clear and effective legislation too many businesses will fail due to cash flow issues.

These CASH FLOW shortages are often caused by allowing a too greater gap between cash inflows and cash out flows—the cash you receive and the cash you have to pay out.

The art of CASH FLOW management is to avoid extended cash shortages.

01 INTRODUCTION

Are you aware of the following headlines within the SME sector: -

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Businesses such as suppliers to retail stores can often wait longer periods of time for their payments, some as much as 120 days beyond the date of delivery of goods. Some such suppliers will offer extended credit, sale or return (SOR) sale or exchange (SOE), marketing funds, point of sale, training support and take a great deal of the stock risk from the retailer.

For example: -

Each business sector will have it's own cash flow issues relevant to it's specific trading patterns and mode of operation.

A cash flow forecast is crucial to ensure cash flow is covered, depicting what cash inflows and outflows are expected under certain conditions over a period of time.

A cash flow forecast should be linked to other forecasts from other business departments—a sales forecast, a production forecast, an overhead forecast, a capex (Capital Expenditure) forecast, a stock forecast, a currency forecast.

Knowing the likely effect on your cash flow position ahead of time helps manage these potential stresses within the business, allowing corrective actions to be taken before cash flow issues hit the business too hard.

However other factors including stock profiles, wages, price mark downs, stock shrinkage, seasonality, credit facilities, overheads, currency fluctuation, competitor activity can all adversely affect cash flow.

Yet all businesses have fixed and variable costs to take in to account. Ÿ This is why a cash flow forecast is so important to businesses and business owners who should have this to hand at all times and be aware of the issues in their particular business that will stress their cash flow.

A retail store will normally deal in cash and card payments, its customers buy product and pay for that product at the point of purchase, this could / should indicate a positive cash flow position. 02 THIS BOOK WILL HELP YOU AND YOUR BUSINESS

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Key actions that most businesses can take to improve Cash Flow issues:-

STRATEGY 1—INCREASE YOUR REVENUES

Outwardly this is often seen as harder to do than to say, however there are a number of tried and importantly tested ways to do this, where the benefits and risks can be calculated.

All of the elements to increasing your revenues have to be taken in to consideration. And this is where the business principles need to have a good understanding of their business functions as well as looking at and taking into consideration all of the internal and external factors that will come in to play in the decision making process.

When looking to increase your revenues you should consider the following: -

03 CASH FLOW ACTIONS

Is the current profit level you are attaining sufficient for the needs of the business?

Will you have to purchase more stock to fulfil increased revenues? Ÿ Will your staff costs increase to fulfil increased revenues?

The fact remains that with a solid and calculated pricing strategy it is possible to increase prices. Gone are the days, or so they should be that an arbitary mark up or margin calculation will suffice in today's modern and competitive landscape.

A price increase strategy can be calculated to show what effect it will have on your volume and what effect it will have on your profitability and your cash flow over time.

The truth is that a small price increase will have little effect on business, in fact a competitive analysis will often shine a light in this once dark area of pricing strategy. See our Pricing Strategy Guide

POSITIVE ACTIONS TO CONSIDER

Should I increase my prices?

Ÿ In reality most business can increase their prices however there is often a perceived fear of taking this action. Most business principles will have a feeling that they probably should increase their prices but at the same time will sight losing clients, competitive position, and current economic climate as reasons not to increase prices.

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A price increase should increase profit but as previously mentioned you need to take other considerations in to play and its is key to have accurate data. Fortunately in the days of online accounting the data needed to decide on the right strategies for your business are much closer to hand and can be manipulated in a variety of ways—but the old adage is still true of quality data in quality data out.

The following guide will help you to understand the net effect of a price increase:-

Often a price increase needs to be part of a bigger strategy and business review.

Other considerations to make in your strategy could include : -

The SLA could include a guarantee—something that your client would see as valuable and a differential.

Every business will have clients that—don't pay on time, make more demands on your business, display limited loyalty, spend less than other clients—could you afford to lose these clients as part of your price increase?

An improvement in SLA's Service Level Agreements, whereby you identify how you can deliver products and services to your client that will be of added value—thus allowing a price increase.

STRATEGY 1—INCREASE YOUR REVENUES-cont'd 7% 2% 6% 5% 5% 4% 4% 4% 3% 14% 4% 12% 10% 9% 8% 7% 7% 6% 19% 6% 17% 15% 13% 12% 11% 10% 9% 24% 8% 21% 19% 17% 15% 14% 13% 12% 29% 10% 25% 22% 20% 18% 17% 15% 14%

Current Margin (your sales could fall by the following % before your GP reduces)

Price Increase 25% 30% 35% 40% 45% 50% 55% 60%

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There are various stock sell through profiles that show the challenges of having the correct stock available—we can categorise these in to:-

The ability to increase the speed at which cash flows are numerous yet some or all of them can have a dramatic effect on your cash flow position.

A. STOCK MANAGEMENT

Careful stock management is a key tool to improve and speed up cash flow. Consider the issue of redundant stock or indeed slow moving stock. Often this stock has tied up your cash for sometime, often having been paid for some while ago. Without a careful eye on your customers stock profile and needs stock can build up, and often without full commitment from the customer.

STRATEGY 2—INCREASE THE SPEED AT WHICH CASH FLOWS

—those who are aware of the latest gadget or The mass adopters item but have made a conscious decision to hold off their purchase until the price has fallen to a more acceptable level.

—those who buy up ends of line, stock The bulk clearance buyer that may be close to the end of its shelf life or where the market is in a state of over supply.

—those who want the latest gadget or item as soon Early adopters as it becomes available—often the mostly costly point of the items life.

Close out stock should be seen as an opportunity to sell it on immediate payment terms and not on credit terms.

Often selling a bundle will help move redundant stock on.

WIGIG deals —When It's Gone It's Gone. Building a "stock provision" within the accounts.

A discount matrix with volume based pricing geared to the stock volumes.

Offering a "Kit" of different but related products. Ÿ A BOGOF deal—Buy One Get One Free.

Regular stock takes to identify slow moving/redundant lines.

Turning slow moving stock in to cash by moving it out can be a sensible approach, the new cash allows for the purchase of fresh stock and can free up storage space.

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B. IMPROVE SALES VOLUME

This type of activity, especially cash with orders, on delivery or proforma orders will mean that the cash moves in to your business and avoids the need for credit terms and credit risk.

These should include viewing your volume purchase based clients, their order patterns and inbound stock needs and preparing an improved offer for larger orders placed. These offers should include speedier payment terms to get their cash in to your business, thus improving your cash position.

C. HOW TO MAKE CUSTOMERS PAY QUICKER

It follows that the opportunity to get customers to pay sooner is also a key strategy to improve cash flow.

Looking for ways to improve sales volumes can improve the speed at which cash flows.

Review the client order process and purchasing decision process

Review the methods that you can receive orders, telephone, email, online, etc—making the process as easy as possible for your clients is key.

Can the client place an order schedule with you and place forward orders.

This will ensure their stock availability and improve your stock planning and by inference your cash flow.

Make sure that your clients are kept up to date with your product codes, descriptions, ASIN's, inner and outer carton quantities

Again work creatively and consistently on the added value offers your provide to your clients .

Ensure your quotations are delivered on time and follow up to "close" the order /deal.

Not delaying invoicing or waiting to batch invoice at the end of the week or month

Invoice the customers at the earliest opportunity.

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D. CLIENT CREDIT APPLICATION AND APPROVAL

Sufficient and up to date credit information is readily available through a variety of approved credit bureaus—these will suggest a credit level and advise on payment history.

An obvious one but a key consideration is to ensure that the invoce holds all of the information needed to allow it to be passed for payment immediately.

It is essential to map this process form start to finish and ensure all participants in the process are fully trained and have associated KPI's (Key Performance Indicators) in place.

A credit application form should be given to every prospect client ahead of any orders being placed—how many times have we seen suppliers pressurised in to delivering goods with out the due process of the credit application approval. This is a significant risk.

Trade references should be taken as part of the account opening process, but be aware that it is common practice for business to pay a few clients on time and giving these as references, to show the best possible payment practice.

It has never been easier to make informed judgements in respect to relevant credit limits.

Most online accountancy systems allow for automatic email reminders to be actioned and set to encourage clients to pay to terms, they can be scheduled as appropriate.

Often initial orders are placed on a C.O.D. basis—Cash on Delivery, this will also include bank transfer, credit card payment, online payment, and are cash risk limiting.

Afterall one risk of poor cash flow can mean wages are paid late therefore it is essential training, recognition and staff buy in to the process is key.

Speed of invoicing is key and every delivery to account holders should be an automatic process as soon as the goods leave the premises.

Include specific information including the due payment date, any discount for early payment and the early payment date –actual due dates should leave no room for excuses.

A crucial part of the order process is to install a sense of urgency in to the people and process and to maximise the efficiency of order receipt and handling.

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E. USE OF AGED DEBTOR REPORTS

The use of Aged Debtor reports is a key tool—every business needs to know who owes what, when it is due and if payment is late why it is late.

Most software packages will give you this as part of the system and can be part of your daily dashboard.

Mapping this process to key individuals within the business is an essential part of good housekeeping.

Accurate note taking is a key activity especially when married to appropriate actions.

Further more a procedure needs to be in place on a debt that has gone past it's due date and parameters detailed based on key time lines and key actions.

There are numerous high profile low cost and often automated debt chasing services available and these can be used at the appropriate time, a time before the debt goes bad.

These will include time lines for phone calls to ask why payment has not been made—this allows any issues to be dealt with early in the process—when payment will be made—this should bring out any issues such as the person responsible for payments is off sick, on holiday etc and appropriate escalation requests can be made.

Most clients will agree to payment terms, some will abide by them but others will operate outside but these will soon become obvious and will need to be monitored.

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F. HOW TO PAY EXPENSES MORE SLOWLY

Again it is key to have supply lines open and not jeopardised by late payment.

Negotiation with suppliers to extend payment terms can dramatically improve cash flow and its often a surprise how accommodating some suppliers can be in this area.

Any bonus or commission payments should only be based on monies received in payment against a particular invoice—it makes little sense to pay against the invoice.

Often companies will arrange to pay bonuses and commissions a clear month after they receive payment to allow for the correct calculation and any disputes to be dealt with will soon become obvious and will need to be monitored.

Asked in the right manner with the facts behind your position is good practice as it is to diarise this process and to review it regularly.

Its an obvious statement to make but paying you suppliers at the last day within the terms agreed means that you hang on to that cash for the maximum period.

Having multiple sources of supply may assist you in having alternative trading terms.

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G. PERFORM COMPETITIVE ANALYSIS

Other considerations should include, warranties given, tech support service, ease of communication, payment options, sales support, field service and support, marketing support.

Managing other expenses is crucial as well as how your business processes these expenses on time.

A major opportunity to reduce costs comes from regular review of basic supply lines these include—Freight in & out, premises costs, utilities, stationery, print, travel and marketing.

Be sure to take all costs in to account—some suppliers will ship at different carriage paid levels or values and carriage costs can quickly eat in to your margins.

Competitive analysis is a key strategy—keeping up to date files from your suppliers will help keep you on top of where you will obtain the stock you need at the best price.

Minimum order values often apply, these can be affected by inner box , carton or outer pack quantities.

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H. BALANCING COST OF STOCK AND STOCK TURN

This process can be used for your suppliers to bid for your business—a number of key suppliers to your business can be engaged in a bid for your business, ensuring a competitive offer and at the same time minimising the amount of your resource needed to manage your purchase agreements and supply chain.

The cost of stock and your stock turn is a key balance to be made. Often it is the case that stock will build up and become redundant or slow moving tying up your cash and without positive and proactive management it will remain taking up space. Often described as the corner of the warehouse where you don't want to turn the light on.

This is a particular problem if your stock is subject to sell by or use by dates.

A FIFO stock process "first in first out" is a good bench mark to use making sure that the stock rotates in the correct way, thus maximising and optimising your stock turn.

Inventory / COGS (cost of goods sold) x 365 = days it takes to turn inventory.

Stock rotation and stock turn should relate to the business sector—for example a horticultural retail seed company will have a short but high activity period selling packets of seeds in to garden centres and retailers who will promote sales during the spring planting season—whereas a protective glove supplier will sell gloves all year around—both business will need to have stock profiles to match their clients demand but each will are likely to have different cash flow requirements.

The use of tenders to engage suppliers is an additional process to be aware of and these can range from the traditional MOD and Health Care tenders through to the more modern e-auctions where a number of suppliers bid on line against a defined purchase volume requirement.

Often savings can be made by shopping around and reviewing current arrangements in areas such as banking charges—many offer free periods at the end of which charges apply and add to cost and affect cash flow.

The same is true for your utility bills—how many people and businesses do not review or change regularly and stick with the same supplier for years. Whilst this is a changing environment it is still not optimised by many people and indeed many businesses.

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I. HOW TO SPEND LESS

Staff wages are often a high cost to businesses, especially in the start- up/development stages and these hiring's should be planned in to the growth and development of the business.

The outsourcing economy is massive and very well developed and there are numerous quality assured sites that you can outsource tasks to at surprisingly affordable prices.

Out right purchase versus leasing capital equipment is an other area to consider, the effect on cash flow can be quite considerable - for example cars can be leased in effect with a balloon payment. Best check with your accountant in this respect.

Review current expenditure against projected expenditure at least each quarter.

One majorly overlooked business expense reclaim is R&D tax relief—where a business can reclaim tax against research and development costs—again this can be outsourced to specialist companies who will often work on percentage fee of the tax reclaim achieved.

With a plan for the business you can monitor and review your time lines and cost introductions without a plan for the business you risk un- necessary expenses and expenditure.

Renting out spare space in your premises can deliver extra income and help with cash flow—this needs to be inline with your obligations to your rental agreement but if you own the property is probably less cumbersome to do. However a check with the mortgage company may be prudent.

Other outsourcing services can also save time as well as improve efficiencies—such as out sourcing the reception duties and the phone answering system all of which may avoid having to hire extra staff and are usually payable monthly with limited tie time lines.

In fact a business consultant can be one of these outsource opportunities—it can be viewed as hiring someone who would command a high salary package at a fraction of their true market costs and take advantage of high level experience and skill sets.

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J. HOW TO VIEW EXTERNAL FINANCIAL SOURCES

Finance loans and overdrafts—banks may require security against personal assets before offering loans or overdrafts and independent advice should be sought prior to accepting these conditions and shopping around for the best deal is vital.

An up to date plan for the business with objective time lines is essential and will be part of any examination of the proposition offered by any institution.

Outside investors range from private individuals through venture capitalists, business angels and crowd funding are all used to assist in business growth. Here you will likely need a professionally prepared investor deck, which can cost £'000's but in the right circumstances provide excellent support, facilities and will run through to agreed exit plans. Equity is also often a cost when entering in to such arrangements especially the more traditional arrangement and "their people" can become part of the businesses management team in some guise.

Factoring is a method of raising money against invoices raised to clients and can fix immediate cash flow issues when entering in to a factoring agreement for the first time. It is key to ensure that you understand the role of the factoring company and that the terms and conditions are achievable for your business.

More and more loan companies in different guises come and go with a few established long term operators advertise for your business. Your accountant and advisors will undoubtedly be able to make introductions, it is advisable to understand if they will receive a commission or bonus payment for the introduction and successful loan facility.

Directors loans—as an owner of a business you can opt to loan the business entity money and register it as a loan.

Not all invoices or indeed all of your customers will be acceptable to the factoring company , but that said they can assist in chasing your clients for payment and manage your aged debtor position within their fees.

In practice you will normally be able to draw on a portion of the invoice at the point of invoice, receiving the balance at a point of complete payment by the client. Any bad debt risk will usually reside with you.

Understanding 3 elements of Cash Flow within your business: -

1. Operating Cash - the cash that flows "In" and "Out" of your business. "In" usually from sales revenues and activity and "Out" usually paying bills and expenses.
2. Cash Investment - the cash that is used for the buying and selling of assets.
3. Cash Financing - the cash used in repaying debts

Remember the old adage that Turnover is Vanity - Profit is Sanity and Cash is King

Many businesses will experience cash flow issues at some point, and these will include profitable businesses. Too many sales can cause a cash flow issue without the correct cash flow forecasts and planning, and this will place stress on the business's survival.

Take your number seriously - be on top of them - seek assistance if needed - understand what they mean to you and how to firstly obtain them and secondly how to manage them.

A Guide to Understanding Your Cash Flow.

ACT Business Consultants Ltd work with SME business owners in Oxfordshire, Wiltshire, Berkshire, Hampshire, Buckinghamshire, and Northamptonshire to build successful and sustainable business architecture. The right tools and processes in place to achieve results based on your objectives.

Should you like to have an initial free of charge discussion to see how we may be able to help you and your business contact us at the following: -

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