

Managing Cash Flow

It's the old story – when business is growing, cash is tight. When it's slowing, cash is tight. The frustrating thing for many business owners is that the company may be profitable but they never seem to have enough cash. As your accountant will tell you, profit is opinion, cash is fact. However, they'll also tell you that cash flow problems may be a symptom rather than the actual problem. You don't have to have cash flow problems. In this article we're going to talk about some simple techniques you can use in the short term, but we'll also look at some of the bigger issues.

There are some immediate things you can do to improve cash flow. Some of these are pretty obvious, but actually implementing them might take some creativity and courage on your part. Your first reaction is likely to be “that doesn't apply to my business”. And it won't, as long as you believe that.

- 📌 Monitor your debtors. Obviously you look at the amounts outstanding after 30, 60 and 90+ days, but here I'm referring to identifying your chronic late payers by name. If they're slow payers, change the way you bill them or stop dealing with them until they've cleared their account. Any worry you might have about alienating them is simply in your head: you're not the one in the wrong, and in any case if you do alienate them they aren't the kind of customer you want. Whatever you do, don't go on providing goods and services to them in the hope that one day they'll pay up. They won't. Instead, one day someone else will take action and you'll find yourself at the end of the queue.
- 📌 Increase your prices. You typically have to lose a lot of business before you start going backwards in terms of profit. Also the income from increased prices goes straight to your bottom line, meaning that when you do get paid, you have a greater buffer to operate on
- 📌 Enforce your terms. Stop lending your customers interest-free money. That's effectively what you're doing when they don't pay you when they should.
- 📌 Tighten up your terms of payment. Most businesses operate on the 20th of the month following, but there is no harm in making your terms 7 days from receipt of invoice. Given what I just said about enforcing your terms, you probably don't want to risk alienating your customer by pursuing them 10 days after the invoice if you know they are regular payers on the 20th. But shortening the term does mean you can legitimately go back to them if you haven't received payment when expected.
- 📌 Free up cash by selling off surplus equipment or getting rid of slow moving stock. There are countless online vehicles for disposing of stuff you don't need – let it go
- 📌 In the same way, buy second hand where possible. One of the things that Venture Capital investors look for is what candidate companies spend their money on – and spending money on new kit when second hand equipment would do the job just as well is one of the warning signs. Remember, quality means “fit for purpose”, not “bells and whistles”.

There are some longer term changes you could make as well. For example, you might consider changing your business model to improve cash flow. When we started in the coaching business, people paid upfront to join the programme. However we've moved to monthly payments for a number of reasons:

- ┌ It's easier for our members in terms of cashflow, so it removes a barrier to entry
- ┌ It provides greater cashflow certainty for us
- ┌ When members see the monthly payment going out they are reminded about the goals they had committed themselves to. They want to make sure they're getting the most out of their investment, so they put more effort into it (and thereby get better results). A recent study showed that people who pay their gym membership monthly use the gym more than those who pay annually

There's a practical example of a change to a business model being in everyone's interests. You may be able to "unbundle" your product or service and get early or progress payments, Other businesses do things like require deposits to cover things they call engagement, establishment, setup costs, sign-on fees, retainers etc. Whatever you call it, ensure it gives the impression that this is a downpayment to secure a priority place in your schedule.

Sometimes poor cashflow reflects poor positioning. People are seldom reluctant to pay when they perceive value, but it's up to us to create that perception. On the one hand we need to make sure that we have happy customers, as they are more likely to pay on time. On the other hand, appearing over-eager to get their business through discounting or special deals gives the power in the relationship to the buyer.

Another form of poor positioning is taking on clients and customers who you know are likely to be poor payers. This is sometimes known as the dance of the desperate. You take their custom because you feel you need the revenue, and they take your offer either because they need it cheap or because others won't supply them. Time spent with low value customers is time you can't spend on high value customers.

All these ideas assume that cash flow problems are a matter of timing. Freeing up cash will create some headroom, but that buffer will soon disappear if:

- ┌ your price is wrong
- ┌ your product mix is such that you're spending a lot of time and effort on small "collects" rather than focusing on the bigger payouts
- ┌ your costs are out of control
- ┌ your marketing system is not producing a steady flow of qualified customers

In other words poor cash flow might be a symptom rather than the disease itself.

Some of this might look too hard. One of my principles is "if it's been done, then it's possible". A few months ago I was talking to a guy who had bought a specialist engineering

company. His worst customer in terms of pricing and payment was unfortunately also his biggest, accounting for 25% of his revenue. After a few months, he went to the customer and said “this is the price, this is the payment date, and here is the setup fee”. The customer had a somewhat negative reaction to this (we’ll leave out the expletives and physical threats) and vowed to never deal with our man again. But our man remained resolute. He was able to fill the workshop with better priced work that he hadn’t been able to take on in the past because the D class customer had always taken most of his capacity. Turnover, profit and of course cashflow all improved immediately. And after a few months, the customer started (very quietly) putting work his way again because no one else could match the convenience and quality. Funnily enough the previous owners had always competed on price, when what their customers really valued was something else entirely. If they’d realized that, they would have got a much better price for their business when they sold.

Tight cash flow is often a symptom of a struggling business in the early days. But it gives us an opportunity to look at the health of the whole business, and identify ways we can improve it. The thing to remember is that responsibility for cashflow rests with us, not our customers or our staff or our business. When we own the problem we can start doing something about it.

This article first appeared in Westpac’s “Good Business” magazine.

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