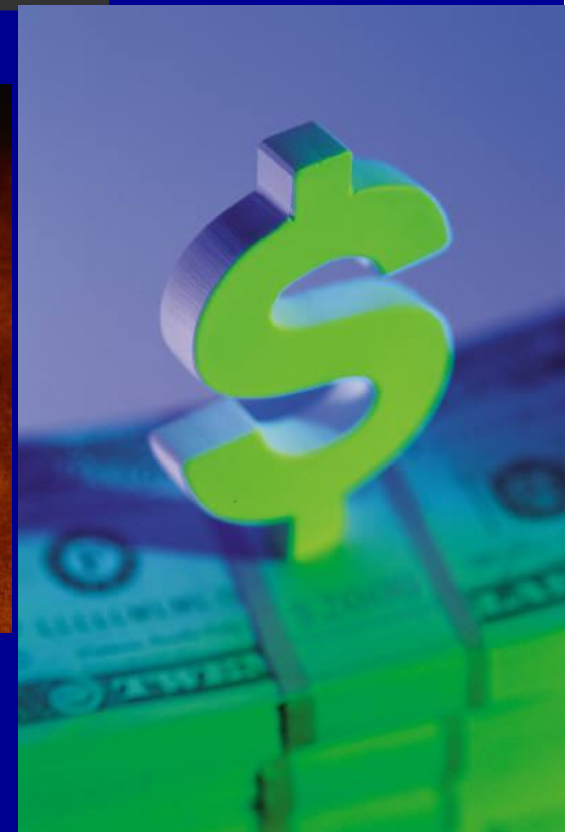


Managing Cash Flow

Presented by
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Basic Financial Reports



- **Balance Sheet** - estimates the firm's worth on a given date; built on the accounting equation:
$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$
- **Income Statement** - compares the firm's expenses against its revenue over a period of time to show its net income (or loss):
$$\text{Net Income} = \text{Sales Revenue} - \text{Expenses}$$
- **Statement of Cash Flows** - shows the change in the firm's working capital over a period of time by listing the *sources* of funds and the *uses* of these funds.

Basic Financial Planning

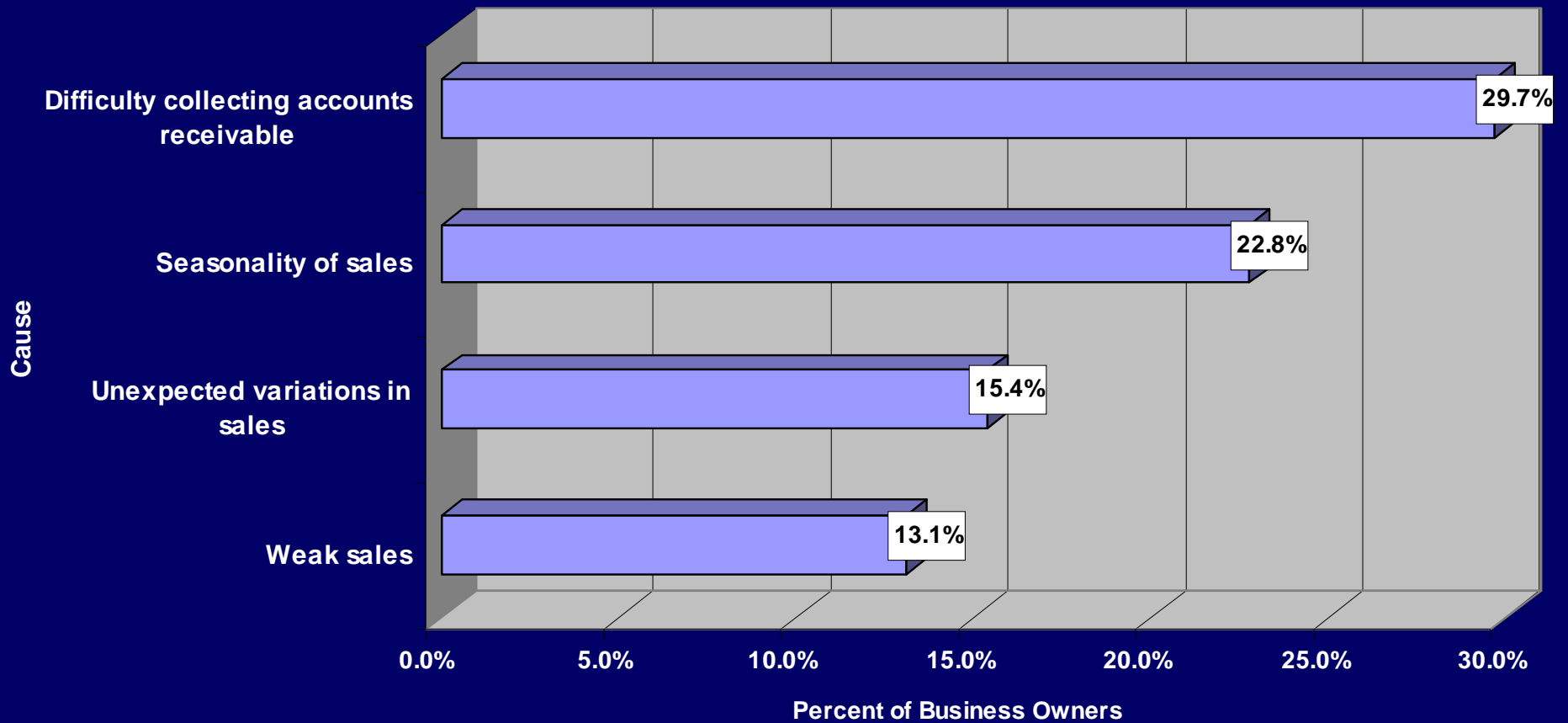
- One-third of entrepreneurs run their companies without any kind of financial plan!
- Only 11 percent of small business owners analyze their companies' financial statements.

Cash Management

- Young, growing companies are “cash sponges.”
- A business can be earning a profit and be forced to close because it runs out of cash!
- Cash management – forecasting, collecting, disbursing, investing, and planning for the cash a company needs to operate smoothly.



Causes of Cash Flow Problems Among Small Businesses



Cash Management

- Geneva Business Bank study: Greatest potential threat to cash flow occurs during rapid growth.
- Study: 68% of small businesses perform no cash flow analysis at all!
- First step: Understanding a company's *cash flow cycle* – the time lag between paying suppliers for merchandise and receiving payment from customers.



Five Cash Management Roles of an Entrepreneur

- Cash Finder
- Cash Planner
- Cash Distributor
- Cash Collector
- Cash Conserver



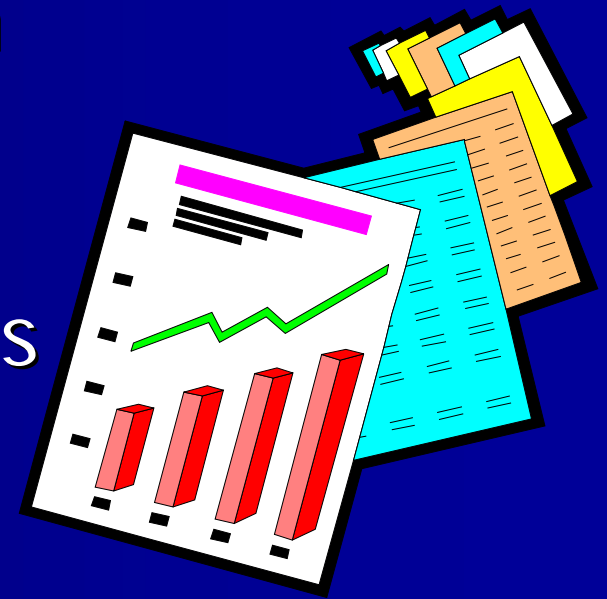
The Cash Budget

- A “cash map,” showing the amount and the timing of a firm's cash receipts and cash disbursements over time.
- Predicts the amount of cash a company will need to operate smoothly.
- A helpful tool for visualizing the firm's cash receipts and cash disbursements and the resulting cash balance.



Preparing a Cash Budget

1. Determine a Minimum Cash Balance
2. Forecast Sales
3. Forecast Cash Receipts
4. Forecast Cash Disbursements
5. Estimate End-of-Month Cash Balance



Determine a Minimum Cash Balance

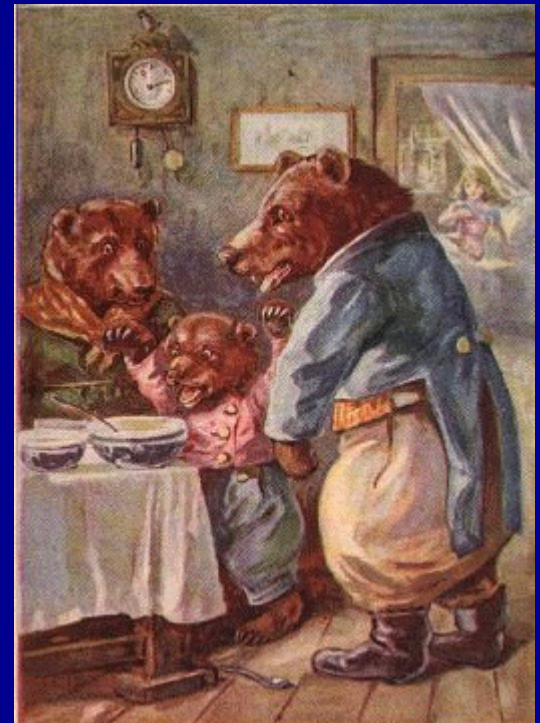
Remember Goldilocks, the Three Bears, and the porridge:

Not too much...

Not too little...

but a cash balance that's just right

... for you!



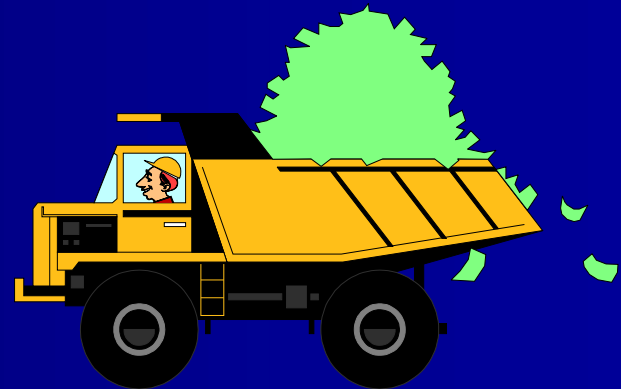
Forecast Sales

- The *heart* of the cash budget.
- Sales are ultimately transformed into cash receipts and cash disbursements.
- Prepare three sales forecasts:
 - Most Likely
 - Pessimistic
 - Optimistic



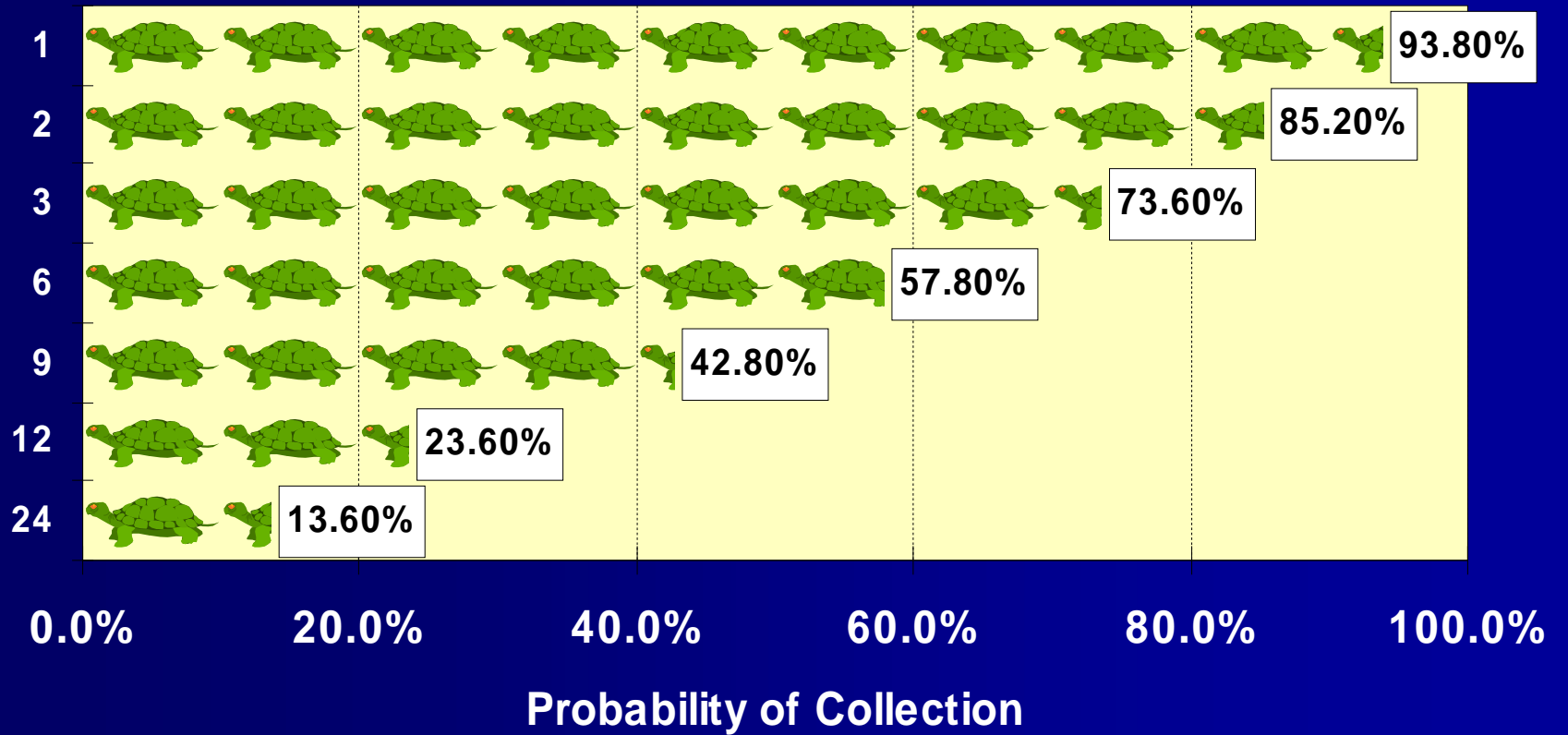
Forecast Cash Receipts

- Record all cash receipts when *actually received* (i.e. the cash method of accounting).
- Determine the collection pattern for credit sales; then add cash sales.



Collecting Delinquent Accounts

Number of Months
Delinquent



Forecast Cash Disbursements

Key: Record cash disbursements *when you will pay them*, NOT when you incur the obligation to pay them.



Forecast Cash Disbursements

- Start with those disbursements that are fixed amounts due on certain dates.
- Review the business checkbook to ensure accurate estimates.
- Add a cushion to the estimate to account for "Murphy's Law."
- Don't know where to begin? Try making a *daily* list of the items that generate cash and those that consume it.

Estimate End-of-Month Balance

- Take Beginning Cash Balance...
- Add Cash Receipts...
- Subtract Cash Disbursements
- Result is Cash Surplus or Cash Shortage (Repay or Borrow?)



Benefits of Cash Management

- Increase amount and speed of cash flowing in
- Reduce the amount and speed of cash flowing out
- Develop a sound borrowing and repayment program
- Impress lenders and investors
- Reduce borrowing costs by borrowing only when necessary

Benefits of Cash Management

- Take advantage of money-saving opportunities such as cash discounts
- Make the most efficient use of available cash
- Finance seasonal business needs
- Provide funds for expansion
- Plan for investing surplus cash



The "Big Three" of Cash Management

- Accounts Receivable
- Accounts Payable
- Inventory



Accounts Receivable

- About 90% of industrial and wholesale sales are on credit, and 40 percent of retail sales are on account.
- Survey of small companies across a variety of industries: 77% extend credit to their customers.

Accounts Receivable

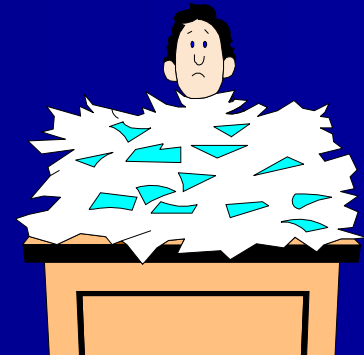
- Remember: "A sale is not a sale until you collect the money."
- The goal with accounts receivable is to collect your company's cash as fast as you can.



Beating the Cash Crisis

Accounts Receivable

- Establish a firm credit-granting policy.
- Screen credit customers carefully.
- When an account becomes overdue, take action *immediately*.
- Add finance charges to overdue accounts (check the law first!).
- Develop a system of collecting accounts.
- Send invoices promptly.



Accelerating Accounts Receivable

- Ask customers to fax or e-mail orders
- Send invoices when goods are shipped
- Highlight the due date on invoices
- Restrict customers' credit until past-due bills are paid
- Deposit checks and credit card receipts daily

Accelerating Accounts Receivable

- Identify the top 20% of your customers and monitor them closely
- Ask customers for up-front payments
- Watch for signs that a customer may be about to declare bankruptcy
- Consider using a lockbox service
- Track the results of your company's collection efforts

Beating the Cash Crisis

Accounts Receivable

- Stretch out payment times as long as possible without damaging your credit rating.
- Verify *all* invoices before paying them.
- Take advantage of cash discounts (e.g., "2/10, net 30").



Beating the Cash Crisis

Accounts Payable

- Negotiate the best possible terms with your suppliers.
- Be honest with creditors; avoid the “the check is in the mail” syndrome.
- Schedule controllable cash disbursements to come due at different times.



Beating the Cash Crisis

Inventory

- Monitor it closely; it can drain a company's cash.
- Avoid inventory overbuying. It ties up valuable cash at a zero rate of return.
- Mark down items that aren't selling.
- Schedule inventory deliveries at the latest possible date.
- Negotiate quantity discounts with suppliers when possible.



Avoiding the Cash Crunch

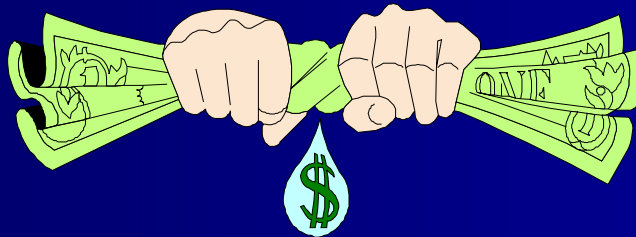
- Consider bartering, exchanging goods and services for other goods and services, to conserve cash.
- Trim overhead costs. For example:
 - Lease rather than buy
 - Avoid nonessential cash outlays
 - Negotiate fixed loan payments to coincide with your company's cash flow



Avoiding the Cash Crunch

(Continued)

- Trim overhead costs. For example:
 - Buy used equipment
 - Look for simple ways to cut costs
 - Hire part-time employees and freelancers
 - Develop an internal security system



Avoiding the Cash Crunch

(Continued)

- Trim overhead costs. For example:
 - Develop an internal security system
 - Devise a method for fighting check fraud
 - Change shipping terms
 - Switch to zero-based budgeting
- Keep your business plan current
- Invest surplus cash

