GUIDE

Avoid running out of money

A business can survive for a short time without low sales or profits, but not without a positive cash balance. It's cash that pays the bills and allows trading to continue and if you are growing and extending credit to more customers, the need for cash can be even greater.

Since cash flow issues can cripple a business, the more warning you have of peaks and troughs, the more time you have to deal with them.

The first step is to find out how likely this is based on your current business. Using our cash flow forecast template, plot out your current expected sales and expenses for the next 12 months. Then apply a 25%, 50%, and 75% reduction in sales, along with any corresponding reduction in expenses or inventory to see what happens to the bottom line.

There are a number of ways to reduce the chance your cash flow goes into the red.

Monitor key warning signs

Decide which profit warning signs hint at a deteriorating cash situation. Comparing short-term performance measures to the long-term cash forecast can quickly reveal if sales and profits are going to plan. For example, you could monitor every month your gross profit margin to ensure it's not slipping which could be caused by:

- Increase in raw materials or product costs
- Reduction in sales
- Discounting
- Wastage
- Increase in customer returns
- Late paying customers

Select two or three key warning signals that matter to your business, set up regular monitoring and then remedy any decline.

Improve operational efficiency

Consider how your business can operate more cost-effectively while maintaining or even improving its efficiency. Take time to document every step of your business process and identify any roadblocks or bottlenecks that make it harder or slower to complete work. Anything you can do to unblock these issues will improve your capacity to do more with less.

Non-Financial Red Flag Warnings

Develop red flag systems on less obvious signals to warn you as often it's not the sudden loss of sales that hints at trouble ahead. Warning signs could be customers are taking longer to confirm a sale, there are fewer phone queries, less web traffic and social media activity or lower foot traffic.

Use Accounting and Cash Flow Software

Accounting software allows you to access information coming straight from your bank account on a daily basis. If you haven't already, sign up for accounting software (ask your accountant which they recommend).

Request progress payments

When negotiating contracts with customers be aware of setting payment terms that help your cash flow, such as deposits or progress payments. Include a regular timetable for customers to pay invoices as part of any agreement and agree on clear milestones for the work to be completed to minimize the chance of the customer disputing any invoices.

Invoice immediately

Make sure all your work is invoiced for as soon as possible and with larger customers you should try to get into the customer's payment cycle or apply to be an approved supplier as soon as possible. Offer immediate payment options that allow you to accept payments via your phone or credit card.

Tighten credit control

An efficient credit control system speeds up your cash collection and reduces bad debt by limiting how much credit you provide customers. Consider using credit scoring systems and setting appropriate credit limits to avoid giving any customer more credit than you could afford to lose if the sale turned into a bad debt. Also, consider:

- Credit check all customers
- Monitor late payments
- Pursue people who owe you money
- Charge interest on late payments.

Using a debt collection agency or a specialist lawyer can be an effective method of dealing with non-payers. There are also software solutions that integrate with your accounting software.

Manage inventory carefully

If you hold inventory then tight controls can help your business hold just enough to service your customers on an on-going basis. Identify seasonal peaks and troughs, set a target stock-turn and sell off any slow-moving, old or obsolete inventory.

It is important to be aware that even if you are profitable a lack of cash flow can still significantly harm your business. Have contingency plans in place to access cash in reserve to survive any crisis and audit your business to identify what could be turned off, re-used, cut down, saved or improved.

Finally, if you always have weekly sales higher than your weekly expenses, you'll never run out.

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