



UNDERSTANDING CASH FLOW

“In the business world, everyone gets paid in two coins: cash and experience. Take the experience first; the cash will come later.” Harold S. Geneen

The best way to explain the concept of **cash flow** and how important it is for good business economics is to think of blood running through the body’s circulatory system. Just like blood, constant, consistent, plentiful and uninterrupted cash flow is critical in order to keep a business in good financial health. More businesses fail due to lack of cash flow than for lack of profit.

Businesses usually start to operate with an initial cash injection by either owners or shareholders, but this one-time cash injection is far from sufficient. Regardless of whether it would be for business expansion or shortage of liquidity, businesses need subsequent regular injections of cash. These cash injections can come from owners’ personal sources, shareholder capital, investors and most often from financial institutions. In order to start an operation, a company needs to start trading its products or services, so it may obtain raw materials or services on credit from its suppliers. It may

also need to acquire fixed assets such as real estate, machines, office equipment and other assets in order to hire people and develop processes. The immediately apparent “issue” with these assets is that they turn an ultimately liquid asset such as cash, into an illiquid one.

Cash also flows out of the business in the form of salaries and wages and maintenance costs such as stationary and insurance. It is only after the company has created a final product or sold a service that money starts flowing back into the business. Other than regular business expenses, cash flow is negatively affected by taxes, repayment and interest on borrowing, dividends and other rewards to shareholders.

When it comes to the process of cash flow planning, setting up contingencies is key. Companies can use invoice financing with **IPS Invoice Payment System** as a flexible financial planning tool giving access to cash injections whenever payables and receivables are out of sync.

IPS Recommends...

In order to be successful with cash flow planning, you need to:

- **Revise and revisit credit policies**
- **Know the payment trend of your customers**
- **Be proactive in managing your accounts receivable**

After you have implemented this process, you will get any or all of the benefits below:

- **Greater liquidity**
- **Financial power (allowing you to negotiate better terms with your suppliers, to be more competitive and to maintain good stakeholder relationships)**
- **Reputation and stability**



CASH FLOW AND CREDIT

The way credit is managed in an organization is extremely important. Managers need to understand the relationship between credit and return on capital. Some managers are more concerned with turning over capital as quickly as possible than making an additional return on capital already made available to customers.

1. Credit Policy administration

Regardless of how many resources you can assign to your credit policy administration, you need to make sure that your credit policy doesn't negatively affect sales reps' relationship with their customers and that it allows sales reps to monitor if the sales they are making are within the terms of your credit policy.

2. Bad debts

Did you know that if you made 100,000 dollars in net sales and had to write-off 1,500 as a result to bad debt, assuming you make 1.5 percent on your net sales, you basically LOST all your profits? This is an unfortunate scenario which involves hidden costs, and as a result to it, a lot of companies get into financial trouble. This cost is even bigger than it seems. Assume you had to hire a collections person who spent several months on the case. This cost is hard to estimate and makes the

bad debt situation spiral out of control. Therefore, in most cases, companies are better off with outsourcing this function to companies who specialize in management of receivables like **IPS Invoice Payment System**.

3. Granting or extending credit

Every time you grant/extend credit, it is important to ask these questions:

- Do you invest the time to methodically check references for your new customers?
- Do you check/re-check customers' financial standing once they placed their first order or increased their purchases?
- Do you check references by phone? Suppliers may tell you things over the phone that they wouldn't put in writing.

4. Credit control and collection

Here's what you need to consider about collections and credit control:

- How fast do statements reach your customers at the end of the month?
- Do you have a set procedure about following-up on outstanding debt?
- Are you proactive in the way you manage your lending on credit terms?
- Do your customers take longer than your credit terms to pay?

Did You Know?

IPS Offers Many Convenient Options for Payment of Your Invoices.

- Online Banking
- Cheque By Mail
- Direct Deposit



INFOPAYS is a monthly newsletter published by **The IPS Business Owner Success School**. The goal of this publication is to provide business owners with quality information on most of today's business management topics in order to help them create and sustain growth.

For more articles, please visit

www.invoicepayment.ca/newsletter.htm

