WHEN YOU'RE THINKING ABOUT CASH FLOW THERE'S PLENTY TO TALK ABOUT

Westpac
Business Bank

“THE MORE MY **ASSETS GROW,** THE MORE MY **CASH FLOW GROWS**”

ROBERT T. KIYOSAKI

ROBERT T. KIYOSAKI (1947 –), BORN AND RAISED IN HAWAII, IS A WRITER AND MOTIVATIONAL SPEAKER. HE SPECIALISES IN THE AREAS OF PERSONAL FINANCE, INVESTING AND BUSINESS. HIS ***RICH DAD, POOR DAD*** SERIES OF BOOKS HAVE SOLD MILLIONS OF COPIES WORLDWIDE AND HAVE ESTABLISHED HIM AS AN AUTHORITY ON PERSONAL WEALTH CREATION.

TALK ABOUT

FOCUS ON

THE LIFEBLOOD OF YOUR BUSINESS

CASH IS THE LIFEBLOOD OF ANY BUSINESS. WITHOUT IT YOUR BUSINESS WILL DIE.

Of all the reasons as to why businesses fail, insufficient cash flow is one of the most common. Often this is not due to the lack of actual business or the amount of sales being made but the mismanagement of the funds available. Every business has its differences, but the core principles are the same, cash is the lifeblood of your business, without proper cash flow management and planning your business will die.

DIFFERENCE BETWEEN PROFIT AND CASH

It is important to understand that profit and cash flow are two different things. Many operators will tell you that it is possible for a business to generate strong profits but collapse because they have run out of cash. The easiest way to explain this is to imagine a business whose profit and loss statement showed that last year they made a profit of $50,000. What the profit and loss statement doesn't show is that for the first eleven months of the year this business was strapped for cash and nearly went under as they only made enough sales to cover their costs. In the last month of the year they made a couple of large sales and this is what resulted in the annual profit of $50,000. Profit is the result of trade over a given period, cash flow is required to keep the business in operation by covering day to day expenses. This is why it is important to manage and understand how cash flows through your business.

WHAT IS A CASH FLOW BUDGET?

A cash flow budget simply records the amount of money that you expect to flow in and out of your business over a given time frame. It is a financial tool that will help predict the availability of cash in a business at any given time. Income and expenses are calculated monthly to help plan for any future short falls in cash.

HOW TO CONSTRUCT A CASH FLOW BUDGET

A cash flow budget is based around a series of assumptions about the expected performance of the business in the future. These assumptions need to be realistic and supported by the most accurate data you have available. If you have access to previous trading results then the best place to start is last years sales and expense records. Allocate these results into similar months that they occurred last year unless you know they will change in the future. You may want to increase sales to account for more growth or you may know that you made an unexpected sale/ expense in a particular month last year that was a one off. You could be looking at introducing a new product line or service, looking to buy a new piece of equipment or employ another person. These will all have an impact on the cash flow budget and are the type of things you should account for so that you can forecast as accurate a picture as possible.

If you plan to use the information on your profit and loss statement understand that these have been prepared for tax purposes and will account for non-cash payments such

as depreciation. This shouldn't be included in a cash flow budget as you don't physically make a payment for these things.

If the business is new, then you will need to base your assumptions on research, market expectations, contracts held, known expenses such as rent or compare other similar business results. The more information you can build into the picture the stronger the tool will be.

Some will say it is a good idea to have three cash flow budgets that account for the best, most likely and worse case scenario. Computer spreadsheets allow you to quickly adjust scenarios and as you receive your actual figures for each month it is important that you fill these in so that you have an up to date position of the business. This will allow you to react as quickly as possible to any changes that may be required. Based on this the cash flow forecast (refer page 14) should be a living document and not filed away and forgotten about. Used properly it is one of the most important business indicators and planning tools you can have.

Many people in business will have their accountant prepare their cash flow budget for them. There is nothing wrong with doing this as long as you, the business owner, understand the information that your accountant has prepared. If you don't understand the assumptions that your accountant has put into the cash flow budget, then you won't be able to use it as an effective tool, and why would you pay to have it done if you are not going use it and just file it away?

THINGS TO REMEMBER

WHY DO A BUDGET?

1. IT HELPS PLANNING
2. IDENTIFIES BORROWING NEEDS
3. SUPPORTS FUNDING APPLICATIONS
4. ALLOWS YOU TO MONITOR BUSINESS PERFORMANCE
5. UNCOVERS POTENTIAL PROBLEMS BEFORE THEY BECOME AN ISSUE

PEAKS AND TROUGHS

THERE ARE MANY WAYS TO GENERATE POSITIVE CASH FLOW – STARTING WITH BEING UPFRONT WTH CUSTOMERS. THE AIM IS TO KEEP THE MONEY MOVING YOUR WAY, RATHER THAN SUBSIDISING SOMEONE ELSE'S BUSINESS.

Once you have completed a cash flow budget it will be apparent as to how much cash you will need, when you will need it and why you need it. You may find that you will generate sufficient cash each month to meet the bills however others may find that their business is seasonal and has some months quieter than others. An overdraft facility is designed specifically for this purpose, to help pay for every day expenses whilst you wait for the cash to come in.

Some business operators believe there is a stigma associated with having to operate with an overdraft facility and that they are not efficient operators. This could not be further from the truth. Many profitable businesses experience peaks and troughs in their cash flow and need the overdraft facility to carry them through these times. The cash flow budget can be used to predict these periods and help calculate the amount of overdraft facility needed. Once the limit is set, the business can use the available funds on a revolving basis within the limit. They will only pay interest on the funds they use eg. If an overdraft limit is $100,000 and the business writes a cheque for $25,000 using the overdraft facility they will only pay interest on the $25,000 until it is repaid in full.

MATCH THE LIFE OF THE LOAN WITH THE LIFE OF THE ASSET

One of the most common problems with the overdraft facility is that it is very tempting to write out a cheque for large items and worry about it later. The overdraft facility is provided to be a source of funds to pay for day to day expenses such as rent, wages, stock, electricity etc. It is not provided to pay for what is known as long term assets. These are things such as cars, office fit out, forklifts, cool rooms, boats etc. Many businesses get themselves into financial trouble because they buy long term assets (they may not be able to afford) by using their overdraft facility. This often uses up a portion of the overdraft facility not accounted for when the limit was set. This is fine when the overdraft funds are not required but when they are the business can come to a sudden halt. It is best to match the life of the asset with the life of the loan. This means long term assets are funded using different types of loans such as leasing and business development loans. Speak to your bank and your accountant about what's the best loan structure for you.

IMPACT OF GROWTH ON CASH FLOW

Experiencing rapid sales growth can be a great thing for business, but it can also be the downfall. It is important to manage growth properly. Many operators in this situation tend to see the sales going sky high, but as they put their hand into the pocket there never seems to be enough cash. As businesses experience rapid growth they are constantly looking to add more services or stock on the shelf to keep up with demand. This demand tends to consume all available cash and a capital injection is

THINGS TO REMEMBER

ACTION PLAN

1. CONCENTRATE ON STOCK CONTROL
2. IMPROVE DEBTOR COLLECTION
3. EVALUATE PRICING
4. MANAGE EXPENSES

often required to support the growth. History shows that it is difficult for a business experiencing such growth to generate sufficient cash internally and may need to look outside of the business for support. There are four key ways that the funding can be sourced. Operators can look for new equity from an outside investor. This involves giving up ownership but could improve expertise. They can use net profits, which is often a limited source of funds and only a percentage of that required. They can use trade creditors within the given terms but again is a limited source of funds and finally they can go a bank.

Among other things a cash flow budget (refer page 14) will help support your case for growth and the need for additional funding.

STOCK CONTROL

If you are starting a business from scratch it is difficult to predict the amount of stock required. You don't want to have too much stock but at the same time you don't want to run out. Things such as the availability of stock, the cost of stock, storage and transport, what contracts are held to fulfil, the nature of the stock whether it be perishable or seasonal such as fashion. How you plan to sell the stock, made to order, or walk off the street.

An existing business faces the same issues except that they have previous trade results to help predict the demand for the following year. These results can be adjusted in line with assumptions about expected changes moving forward and understanding what impacted the business last year.

Some operators tend to hoard stock regardless of how useless and unsaleable it is. They can't help themselves. It is important to understand what the real cost of this stock is to your business and how much cash is tied up in the working capital cycle (refer pages 6–7). Sometimes there is a competitive advantage in being able to provide the right product at the right time but if the stock is old and not needed the golden rule is to get rid of it. Recoup the cash as best you can such as have a sale and inject it back into the business.

Look at what your product mix is, some stock will turn over faster than other items and in general these will have a lower margin but much higher volume. Other items may turn over more slowly but will make a much higher margin. Understanding the relationship between price volume and cost and the impact on your business is covered on pages 10 and 11.

Buy what you need not what you want. Set up a system that manages stock. This may be having one person responsible for ordering or a centralised computer program. Check all stock against the invoices to make sure what you order is what you get and record when it should be paid for and any discounts available.

HOW TO RIDE THE WORKING CAPITAL CYCLE

AVAILABLE CASH TENDS TO GET TIED UP IN WHAT IS KNOWN AS THE WORKING CAPITAL CYCLE (WCC). EVERY BUSINESS, REGARDLESS OF WHAT THEY DO, HAS A WORKING CAPITAL CYCLE.

To start any business, cash is required. This cash is then used to purchase stock in order to generate a sale. When the stock is sold it is either by way of a cash sale or is charged to an account, creating a debtor. When the debt is collected the WCC continues. In a service industry the stock is work in progress.

Imagine that the stock a business buys sits on the shelf, on average, for fifty five days before it is sold and that it takes an average of forty five days to collect the debtors. Each dollar tied up in the WCC takes one hundred days before it returns to the cash position where it can be used again to purchase more stock (refer diagram). While waiting for that dollar to return, more stock has to be purchased to keep the business operating and to do so, many businesses use their overdraft facility which is costing them money. If there is no overdraft, they are using their credit funds that could be better used elsewhere. The faster you can turn the WCC, the faster the dollar returns and the less overdraft or surplus funds you have to use. This is where efficiency in debt collection and improving your stock turnover is the key.

KEEPING YOUR RECORDS

It is critical that you keep good financial records in business. It doesn't matter if they are paper based or on a computer software program but they need to be simple to understand, reliable and accurate. They need to be in a consistent format and designed to provide information on a timely basis.

These records will form the basis of your financial statements and tax returns. Your accountant can help you to determine what records you should keep and what information they should contain. In general you need to keep records of all transactions, accounts receivable, accounts payable, payroll, petty cash and inventory.

Don't get swamped by data. Some people love to produce reports and it is then that it becomes all too much and easy to set aside. Ask

your accountant what you need to measure in your type of business. Set yourself some key performance indicators and produce reports that make sense to you. Things that get measured get managed. If you don't understand, ask the questions – or you may be missing out on opportunities to improve the performance of your business.

COLLECTING DEBTORS

Remember a sale is only completed when your invoice is paid in full. Many people concentrate on making the sale but fail to set up the credit control procedures until they experience a bad debt. These procedures should be in place from the start.

Create a terms of trade policy that can be provided to customers explaining what is expected of them and by you should they not comply by these rules. Don't rest on verbal agreements remember this is business and even the best deals can go wrong.

Consider how you want to be paid and how that can impact the cash flow in your business. If you currently trade on cash only basis and are considering offering terms this should be built into your cash flow budget to determine the impact on your month end cash position. Consider the additional risk to your business, uncollectible accounts, systems and processes. On the other hand if you get it right it may bring you more business opportunities and more customers.

If you have exposure to only a couple of major customers this can pose a risk to your business if they get into financial difficulties. Make sure that you check credit references, that you know who is going to sign the cheques and address the bill to them.

Once the bill is issued you then have to wait for it to be paid.

THINGS TO REMEMBER

MAKING SALES

1. A SALE IS ONLY COMPLETED WHEN YOUR INVOICE IS PAID IN FULL
2. PUT CREDIT CONTROL PROCEDURES IN PLACE TO AVOID BAD DEBT
3. ALWAYS GIVE YOUR CUSTOMERS A TERMS OF TRADE POLICY
4. BUILD CREDIT TERMS INTO YOUR CASH FLOW BUDGET
5. ALWAYS CHECK CREDIT REFERENCES

WHEN THE CHIPS ARE DOWN

THE CASH WAS FLOWING, BUT GARY LEECH'S COMPANY, KETTLE CHIPS, WAS NEARLY FRIED BY THE OLDEST TRICK IN THE BOOK – A CASH FLOW CRISIS.

When I started Kettle chips, we sold through our own distribution network and the money was coming in, but sporadically. I had asked my potato growers if they would wait for payment while we built the business.

They had surplus capacity over what they were already producing for the big chip-makers, so initially they weren't growing specifically for us.

We were not on top of the cash flow cycle. At first this wasn't a problem. But we were selling heaps of product, the business was going gangbusters and, like everyone else in the early stages of a manufacturing business, we thought that if we just kept up the pace, all would be well. After all, our sales had built into millions of dollars within a couple of years.

But suddenly our cash flow cycle blew out. We were exposed with more money going out than was coming in. We had a $750,000 loan and were in a crunch. There were five of us in the company, and some of us had houses at stake. I suddenly learned about debt-equity ratios and the money cycle.

I noticed that one customer owed $50,000. The next time I looked it was $100,000, then it was $250,000.

At one of the first meetings with our new chief executive officer, he just ran his eye down the list of overdue accounts and stopped at one for $5,000. "Collect this or stop supply," he said. Some in the company didn't want to do this. "But he's a mate," they said. "He's been with us since the beginning, you can't do this."

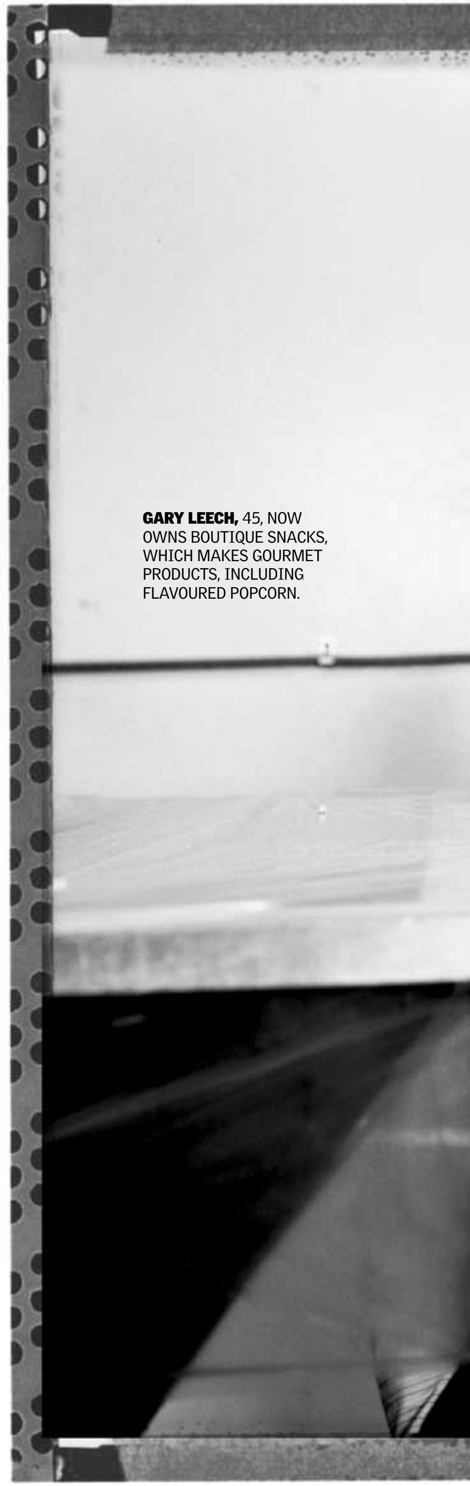
The CEO just said, "Do you want to collect it now or wait until it hits $50,000?"

Of course the debt is harder to pay the bigger it gets. We actually had to write off an awful lot of money while we got our business ship-shape and started to track sales, collect money and pay accounts on time. It's the classic case of a small business growing fast and then having to learn expensive lessons on the run.

But it all came good and within five years we were debt-free and looking at the next phase – further expansion. That would have meant going into debt again, spending $5 million on production facilities as we ramped up. Our advertising budget would have gone from $400,000 to several million. Higher volumes would reduce margins and profits would come down. The law of diminishing returns.

We were doing $18 million in sales with an EBIT (earnings before interest and tax) of $2.2 million, three times the industry average, with a 12 per cent profit margin when others were only at 3 or 4 per cent.

At that point the choice was either to grow bigger with all the hassle and financial risk that entails, or to sell out. After negotiating with several parties, I sold out for $24 million to Arnotts – the company I'd worked for and which had originally rejected my idea for a higher-value, higher-priced potato chip.



GARY LEECH, 45, NOW OWNS BOUTIQUE SNACKS, WHICH MAKES GOURMET PRODUCTS, INCLUDING FLAVOURED POPCORN.

GARY'S TIPS:

- Get your efficiencies in place, particularly around debtor collection and stock turnover, before your business goes into rapid growth mode.
- Lease your machinery. My new company doesn't have its own equipment or plant. I'm not having dead capital again, so we've outsourced production, which responds to demand. If we don't sell stuff, we don't have any costs. I've learned to get a better skew between our fixed and variable costs.
- Build slowly and steadily. We are now building a new distribution network, taking care to choose those people who want to align their personal goals with ours and grow with us.

THE PRICE IS RIGHT

MANY BUSINESS OPERATORS BASE THEIR PRICES ON THE COMPETITION. IN DOING SO THEY ASSUME THE COMPETITION HAVE THEIR PRICING STRUCTURE RIGHT, THAT THEY ARE MAKING A PROFIT AND THAT THEY HAVE THE SAME COST STRUCTURE AS THEMSELVES. IN REALITY EVERY BUSINESS HAS A DIFFERENT COST STRUCTURE AND IT IS IMPORTANT TO UNDERSTAND YOURS.

Some businesses reduce their prices to obtain a greater share of the market with the aim to increase their price later and hopefully end up with more market share than when they started. Unfortunately many who use this approach find out that volume is bought more easily than profits. There aren't many wins with price wars. Those who last the distance are the ones with the least debt, the strongest balance sheet and know their costs.

By understanding your own cost structure you are able to answer questions such as: How many extra sales you have to generate to compensate for a reduction in your price? If you increase your price, you could assume that you may experience a decrease in sales. By how much can your sales reduce before it starts to affect your bottom line? How many sales do I have to make to cover my costs or just break even, ie: the point of no profit but also no loss?

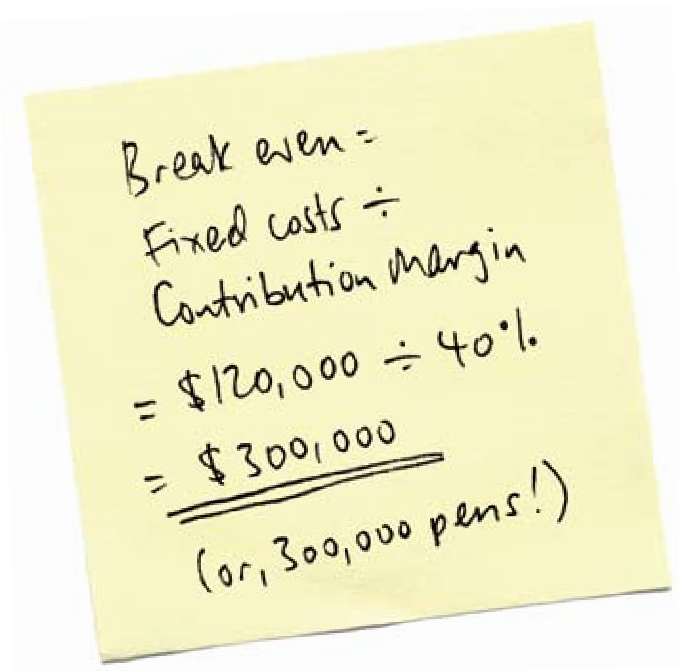
Break even analysis is a financial tool that allows you to work these things out. This sounds like rocket science but in reality it is quite simple. Expenses in your business can be divided into two main categories. The first of these are fixed costs. These are those expenses not directly related to sales ie. they remain relatively constant regardless of the sales volume and includes rent, wages, rates and utilities. All other expenses are known as variable costs and are directly related to the volume of sales, which means for every dollar you make you incur an additional cost eg. stock, materials, direct labour and commissions.

Often it is assumed that every dollar that comes into the business is another dollar to spend on something else. Unfortunately this is not the case. If your rent goes up by $10,000.00 the extra sales required to cover this cost will almost certainly not be $10,000.00 but will be dependant on your cost structure. For example, let's assume I sell pens. These pens cost me sixty cents to produce and I sell them for one dollar. Therefore out of every dollar earned a portion of this is already spent. In this example the variable costs are sixty cents, which leaves me with forty cents in every dollar to contribute towards all other fixed costs. This portion of the dollar is called the contribution margin.

If the total fixed costs in my business add up to $120,000.00, how many sales do I have to make to break even?

If we know that out of every dollar earned we only have forty cents (or 40%) left to pay for our fixed costs

BREAK EVEN ANALYSIS IS A POWERFUL FINANCIAL TOOL WHICH CAN BE USED TO MEASURE THE IMPACT OF A CHANGE IN PRICE, VOLUME OR COSTS AND HELPS YOU PLAN AND DEVELOP STRATEGIES TO REDUCE THE EFFECT OF THESE CHANGES.



and that our fixed costs add up to $120,000.00 then we can work out the sales required to break even thus: This is how many sales are required to break even, the point of no profit and no loss. If the business sold 301,000 pens they have only made a profit of forty cents, because out of every dollar sixty cents has to be spent to produce that pen.

Break even analysis is a powerful financial tool which can be used to measure the impact of a change in price, volume or costs and helps you plan and develop strategies to reduce the effect of these changes. If you are planning to buy a piece of equipment, take on a new employee, pay someone a bonus or want to set yourself a certain profit, break even analysis can be used to show you how many extra sales or additional production is required to cover these costs.

REALITY

LIKE MANY SMALL BUSINESSES DRIVEN BY PASSION, KAREN LEBSANFT, 42, FOUND THAT UNDER-CAPITALISATION WAS THE MAJOR OBSTACLE FOR KURRAJONG KITCHENS.

Lack of resources has never stopped an enthusiastic business owner from launching out into the unknown, but Kurrajong was fortunate in that its fledgling baking business – producing lavosh, biscotti and mini-toasts – was a sideline to a successful restaurant and reception centre business.

Demand for the specialty breads and biscuits has exploded, and today Karen's products are sold in supermarkets and on Qantas business class flights. She speaks highly of the value of education, having done several courses available in the western Sydney area.

Husband Ben, 42, is the production and finance part of the business, with Karen doing the marketing and human resources.

Ben has been cooking since he was 14 and Karen has worked for many years in the hospitality industry, where she had to juggle budgets and use her project management skills.

Their trick of using the restaurant takings to smooth out cash flows in the kitchen came to an end when the baking business overtook the hospitality business. The couple sold the restaurant and sub-leased part of a nearby bakery to increase production until finally they bought the bakery.

With 40 staff and production of 30,000 packets of lavosh and biscotti a week, the business now has some serious cash flow management in place.

Karen has had to "drill down into the figures" to find out which products are making the most money, and which customers are providing the greatest value. This has helped them to better understand the cash flow cycle, and how to calculate their break-even point and focus on maximising profits.

The analysis did not reveal too many surprises, Karen says. But it did bring data to support what she knew from "gut feel" about what was making money and what was not.

"We now do a cash flow forecast as part of our budget process, and watch it on a weekly basis. Then we check at the end of the month through our accounting system that our targets are on track.

She says that prompt debt collection is a key to cash flow management.

"In business it is possible for one supplier to grow at the expense of another, so I have always explained to customers that we are businesses working together for the survival of both. So I tell all customers that the account is due on a certain date and that if it's not paid on that date we will be calling to remind them."

Their company has just appointed a part-time financial controller to manage the next phase of the company growth, which will lead to a public listing.

CHECK

GEOFF MORGAN AND ANDREW BANKS, WHO BUILT AND SOLD A COUPLE OF RECRUITMENT BUSINESSES, ADVISE ON THE CASH FLOW CYCLE.

Karen and Ben have learned on the run what all SMEs go through once they start selling their products. Sales usually aren't the issue – it's the cash flow. Kurrajong Kitchens had cash coming in the door of their restaurant, which got it over this initial hump. Then they had to manage the whole growth process. They have done well in seeking training and professional expertise to add to their obvious business skills.

From the very first days of our business, we had strong systems and processes in place to manage cash flow.

The motto underpinning our attention to financial strength was, "Where attention goes, so energy flows."

Cash is oxygen for businesses. A business might start out with a terrific idea but fail because it runs out of cash. And that could be for a number of reasons. Maybe they didn't get enough from the bank. Maybe they had their foot on the accelerator too hard. In the management services business, you use cash to pay temporary staff, and some of our competitors went broke while we flourished. That was because we managed our cash flow. We billed our clients weekly and were prompt in collecting the cash. So we had good cash flow in an industry that traditionally had negative cash flow – primarily because our competitors had poor systems and did not focus enough on cash collection.

At the beginning, our approach to accounting and finance was simple. There were just seven of us in a small recruiting firm that was strapped for cash, hoping that we didn't go bust. Allen Kime our then part-time accountant (who was 67 and had tried to retire twice) used to bring us a small square of paper on a Friday afternoon that said it all. He listed the following (complete with weekly figures:

Invoiced sales
Cash in
Cash out
Cash balance at bank/overdraft
Number of placements
(people we had put in new jobs)

FROM *FLOURISH & PROSPER*, BY GEOFF MORGAN AND ANDREW BANKS (PENGUIN VIKING)

TRACKING TIPS

KNOWLEDGE IS POWER

1. PUT GOOD CASH FLOW TRACKING SYSTEMS IN PLACE
2. IF YOU TAKE YOUR EYE OFF THE NUMBERS, THE ENERGY WILL GO OUT OF YOUR BUSINESS
3. WORK OUT WHAT YOU NEED TO TRACK – CASH IN, CASH OUT, TURNOVER
4. IF YOU DON'T UNDERSTAND THE NUMBERS, GET AN ACCOUNTANT (EVEN A PART-TIMER) TO HELP OUT
5. MAKE SURE DEBTS ARE COLLECTED PROMPTLY

CASH FLOW FORECAST

USE THIS SAMPLE CASH FLOW FORECAST AS A GUIDE TO TRACKING YOUR INCOMINGS AND OUTGOINGS.

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP
BEGINNING CASH POSITION									
INCOMING									
Cash Sales									
Collections (Accounts Receivable)									
Other income									
A: TOTAL CASH AVAILABLE									
OUTGOING									
Accounts Payable									
Past Due: Accounts Payable									
General Expenses									
Wages									
Monthly long-term debt (principle repayments)									
Other									
B: TOTAL CASH OUTFLOW									
MONTH END CASH POSITION (A - B)									
Short-term loan required									
ENDING CASH POSITION									

OCT	NOV	DEC	TOTAL

COLLECTION TIPS

MANAGING ACCOUNTS RECEIVABLE

1 MAKE PREPARING YOUR INVOICES ONE OF YOUR HIGHEST PRIORITIES

2 HIRE AN EXPERIENCED ACCOUNTS RECEIVABLE MANAGER, AND HAVE THEM FORM A FAVOURABLE RELATIONSHIP WITH THE PERSON WHO SIGNS THE CHEQUES

4 PROVIDE CUSTOMERS WITH INFORMATION ABOUT THE PAYMENT PROCESSES AVAILABLE

5 AT POINT OF SALE IDENTIFY HOW THEY WILL BE PAYING – CASH, CHEQUES DIRECT INTO YOUR BUSINESS ACCOUNT

6 PROVIDE YOUR ACCOUNT DETAILS IN WRITING

7 INCLUDE DUE DATES ON ALL INVOICES SENT OUT

8 IF YOU OFFER A DISCOUNT, MAKE SURE IT IS CLEARLY SPELLED OUT ON THE INVOICE

9 SEND A STAMPED, SELF ADDRESSED ENVELOPE WITH INVOICES

10 CATEGORISE SLOW PAYERS AND DEAL WITH THEM ACCORDINGLY

11 REDUCE THE GRACE PERIOD FOR LATE PAYMENT, AND INCREASE THE FREQUENCY OF REMINDERS TO LATE PAYERS

12 MAKE COLLECTION CALLS EARLY IN THE WEEK. BE PERSONABLE!

13 IF THERE ARE REPAYMENT ISSUES, SUGGEST AN INITIAL DEPOSIT WITH AN ONGOING REPAYMENT SCHEDULE

14 WHEN AN AGREEMENT HAS BEEN REACHED, IMMEDIATELY SEND A FORMALISING LETTER

15 COPY ALL INCOMING CHEQUES. DEPOSIT THE ORIGINALS IMMEDIATELY AND USE THE COPIES FOR RECONCILIATION AND ACCOUNTING

16 PAY SUPPLIERS ON A CHRONOLOGICAL BASIS – RATHER THAN PAYING ALL ON THE SAME DAY

AT A GLANCE

FILL OUT THE FOLLOWING CASH FLOW INVENTORY TO REVEAL THE STATE OF YOUR BUSINESS FOR ACCOUNTING, TAX AND PLANNING PURPOSES.

1 HOW MUCH INCOME ARE YOU GENERATING NOW AND HOW MUCH INCOME CAN YOU EXPECT TO GENERATE IN THE FUTURE? ....

2 HOW MUCH CASH IS TIED UP IN ACCOUNTS RECEIVABLE (AND THUS NOT AVAILABLE TO YOU) AND FOR HOW LONG? ....

3 HOW MUCH DO YOU OWE FOR RENT? MERCHANDISE? UTILITIES? EQUIPMENT? ....

4 WHAT ARE YOUR EXPENSES, INCLUDING PAYROLL, PAYROLL TAXES, MERCHANDISE, ADVERTISING, EQUIPMENT AND FACILITIES MAINTENANCE, AND BENEFIT PLANS FOR YOURSELF AND EMPLOYEES (SUCH AS HEALTH INSURANCE, RETIREMENT, ETC.)? ....

5 HOW MUCH CASH DO YOU HAVE ON HAND? HOW MUCH IS TIED UP IN INVENTORY? WHAT IS YOUR ACTUAL WORKING-CAPITAL BUDGET? ....

6 HOW FREQUENTLY DO YOU TURN OVER YOUR INVENTORY? ....

7 WHICH OF YOUR PRODUCT LINES, DEPARTMENTS OR SERVICES ARE MAKING A PROFIT, WHICH ARE BREAKING EVEN, AND WHICH ARE FINANCIAL DRAINS? ....

8 WHAT IS YOUR GROSS PROFIT? WHAT IS YOUR NET PROFIT? ....

9 HOW DO ALL OF THE FINANCIAL DATA LISTED ABOVE COMPARE WITH LAST YEAR – OR LAST QUARTER? HOW DO THEY COMPARE WITH THE PROJECTIONS IN YOUR BUSINESS PLAN? ....

10 HOW DOES THE FINANCIAL DATA COMPARE WITH THOSE OF YOUR COMPETITORS? ....

CASH FLOW KEYS

1. PROFIT AND CASH ARE TWO DIFFERENT THINGS.
2. PROFIT PAYS BACK LONG TERM DEBT AND SUPPORTS GROWTH.
3. CASH FLOW PAYS FOR DAY TO DAY EXPENSES.
4. EVERY BUSINESS SHOULD COMPLETE A CASH FLOW BUDGET POSITION.
5. PREPARE THREE FORECASTS FOR THE SAME BUSINESS – BEST CASE, WORST CASE AND MOST LIKELY.

CAN I?

COMMONLY ASKED QUESTIONS

CAN I MANAGE MY CASH FLOW SIMPLY BY MONITORING MY BANK BALANCE? No, anticipating future cash flow is important to ensure that you do not miss the implications of an impending cash flow deficit before it is too late.

AS LONG AS I AM MAKING A PROFIT, WON'T MY CASH FLOW TAKE CARE OF ITSELF? No, profits are not cash. Revenues and expenses determine profit, whereas cash receipts and cash disbursements determine cash flow. A profitable business can run out of cash by 'over-trading.'

DO I NEED TO HAVE A CASH FLOW BUDGET? Yes, a controlled cash flow, the end result of cash flow budgeting, will more than repay the time and effort you give to it by ensuring that you can pay your bills when they are due.

WILL THE BANK ASK ME FOR A CASH FLOW BUDGET WHEN I APPLY FOR A BUSINESS LOAN? Yes, because it tells the bank how much money you need to borrow, when it will be needed and when it will be repaid.

DOES MY 'OPERATING CYCLE' AFFECT MY CASH FLOW? Yes, the amount of time your cash is tied up in stock and debtors affects your cash flow. The shorter your operating cycle the less money you need to invest in stock and debtors, whereas the longer your operating cycle the more money you need to invest in stock and debtors.

THE "CAN I" QUESTIONS ARE PART OF A SERIES DEVELOPED BY JOHN ENGLISH FOR THE *TALK ABOUT* SERIES OF BOOKS. ENGLISH, ASSOCIATE PROFESSOR OF ENTREPRENEURSHIP AT THE UNIVERSITY OF CANBERRA, IS A WELL-KNOWN AUTHOR AND CONSULTANT TO SMALL BUSINESS. HE WROTE THE BEST-SELLING *HOW TO ORGANISE AND OPERATE A SMALL BUSINESS IN AUSTRALIA* (ALLEN & UNWIN, NINTH EDITION, 2003).

THINGS YOU SHOULD KNOW

CONTACTS

www.ausindustry.gov.au

www.ato.gov.au

NSW www.smallbiz.nsw.gov.au/smallbusiness
NT www.kakadu.nt.gov.au
QLD www.smartsmallbusiness.qld.gov.au
SA www.southaustralia.biz
VIC www.biz.vic.gov.au
WA www.sbdc.com.au
TAS www.iris.tas.gov.au

Australian Consumer and Competition Commission
1300 302 502 www.accc.gov.au and click on
Franchising to see the Franchising Code of Practice

Office of Small Business (02) 6276 1331
www.industry.gov.au
ACT 1800 244 650 www.business.act.gov.au
NSW 1300 134 359 www.smallbiz.nsw.gov.au
NT 1800 193 111 www.tbc.nt.gov.au
QLD 13 26 50 www.sd.qld.gov.au
SA www.cibm.sa.gov.au
TAS 1800 440 026 www.dsd.tas.gov.au
VIC 13 22 15 www.businessaccess.vic.gov.au
WA 1800 199 125 www.sbdc.com.au

HELPFUL READING

Driving Small Business, Des Knight and
Noel Whittaker (Simon & Schuster, 2002)

Small Business For Dummies, Veechi Curtis
(Wiley Publishing, 2004)

*How to Organise And Operate a Small Business
In Australia*, John English (Allen & Unwin, 2003)

TO DO LIST

HAVE I...

- [ ] PREPARED A CASH FLOW BUDGET?
  See page 2
- [ ] THOUGHT ABOUT THE PEAKS AND TROUGHS?
  See page 4
- [ ] GOT A HANDLE ON STOCK CONTROL?
  See page 5
- [ ] LOOKED INTO THE WORKING CAPITAL CYCLE?
  See page 6
- [ ] GOT A GOOD RECORD-KEEPING SYSTEM?
  See page 6
- [ ] THOUGHT ABOUT MY COST STRUCTURE?
  See page 10
- [ ] INTRODUCED A SIMPLE CASH FLOW FORECAST?
  See page 14
- [ ] COMPLETED A CASH FLOW INVENTORY?
  See page 16
- [ ] ....
- [ ] ....
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TALK ABOUT

To find out how Westpac can help your business, please speak to your Relationship Manager or contact Business Direct on 132 772 (metro), 1300 134 979 (regional).

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