HOW TO MANAGE YOUR CASH-FLOW

Many factors can lead to a business failing, but at the point when it becomes insolvent there is always one common factor: cash-flow. How many companies are forced into liquidation with a healthy bank balance? Good cash-flow management is important during difficult times, but is essential when the economy starts to pick up.

Good cash-flow management is primarily driven from a business' credit control function and the management of debts. To understand the importance of good credit control, consider the following: a company turning over £1 million can increase its cash by nearly £15,000 if it reduced the average number of day's credit given to customers by a mere five days.

Good credit requires established procedures, sound working practices and good communication. The key principles to achieving these are set out below:

Establish a credit policy

Ensure there is an internal policy detailing specific timings for taking action on outstanding debts. This may be a timetable for phone calls, letters and legal action.

Be cautious with new customers

Credit checks should be obtained for all new clients. During initial trading, tread carefully with new customers and be conscious of your exposure. If someone has not paid other suppliers there is a good chance they will not pay you either. If you have any doubts, request payment up front or consider introducing a strict credit limit at the start of the relationship. Alternatively, you can always ask for a third party guarantee.

Communicate regularly with your customer

Issue clear and accurate invoices as early as possible, as this helps avoid uncertainty and ensures any contractual changes are identified early. You should also send statements and reminder letters on a regular basis so that the customer knows you have a consistent approach to cash collection.

Credit control is an ongoing process, so ignore the problem. Should a customer not meet your terms, it is even more important to keep lines of communication open and try to reach an amicable arrangement. This not only keeps cash flowing through your business, but will help maintain relationships with the customer. Legal action should only be taken as a last resort after all other communication has failed.

Establish a separate credit control function

Where possible, create an independent credit control function. If the size of the business permits, it should be separate from the regular customer management. It is easier to look objectively at the level of debts if you are not directly involved in the client relationship. It is also easier for an independent party to chase the debt.

Regular reviews

Aged debts should be reviewed on a regular basis to identify accounts that need to be chased. Undertake a weekly review – this should prompt regular chasing of balances and debtors.

Credit limits

Establish realistic credit limits for all customers and ensure that they are observed. If a client reaches their credit limit, stop supplying until the debt is cleared. Their need for continuing supplies is your leverage to get outstanding debts cleared.

Monitor clients

Be conscious of customer payments and look for possible changes in patterns that might indicate problems.

Communicate credit terms on invoices

Customers must know what your terms are. Detailing bank details on invoices can encourage direct payments into bank accounts.

Avoid disputes

Ensure invoices are agreed with clients before sending. Some customers will look for excuses to avoid or delay paying bills so that they can hold onto their cash for longer. Set out your terms and conditions in writing. They should cover price, delivery, payment terms and credit limits. They should also state clearly how any dispute will be dealt with. Obtain the customer's agreement to the terms and conditions in writing if possible.

Timely invoices

Customers will certainly not pay until they have received an invoice, so the sooner the invoice is despatched the sooner you can start to chase.

Manage your own your banking and debt facilities

Aside from the credit control function, you can improve your cash flow by managing your own debt.

- Take advantage of any credit facilities offered by suppliers. There is little benefit in paying early unless there substantial early-settlement discounts are offered.
- Your routine planning should forecast your cash balances and ensure any problems are identified early.
- Keep a close working relationship with your bank manager.
- Ensure other elements of working capital are controlled – in particular, make sure you do not hold excessive stock.
- Be aware of breaks that may be available to you. If cash-flow is tight, HMRC may well look favourably on a request for time to pay (either VAT or corporation tax). This is something that the government is trying to encourage.
- Ensure bank facilities are adequate. If your facility is not sufficient and your business is viable there may be additional bank funding available for you.

Should you wish to discuss any of this information further, do not hesitate to contact your Menzies representative or email enquiries@menzies.co.uk.