Finding money within your business

Most small businesses experience cash flow problems from time to time and urgently need working capital. Many business owners immediately think of the bank or loans when they're short of money. But there are other resources you can tap before you ask for that expensive overdraft or overdraft extension. The money you need might already be there—locked up in inventory, assets or your debtors' book.

You can often free up funds from within your business by re-examining your business systems, and these funds might in themselves be sufficient for your immediate needs.

Good management

Even if the funds you free up from within your business are not sufficient, there is another payoff: the effort you make in searching for them helps to ensure that you are running your business in an efficient manner.

To free up funds from within your business, look closely at:

- assets
- customers
- suppliers

Assets

Your assets include debtors, stock, pre-paid expenses, vehicles, plant and equipment, fittings and property. Each of these is a possible source of funds.

Debtors

Are you letting some customers have the free use of your money for months? This is a common occurrence in small businesses where the owner(s) are so busy getting the business off the ground, products out the door, or services completed, that they don't pay enough attention to basic business procedures. Many customers will take advantage of this 'free money'. **But your business is not to serve as a free bank.**

Here's how you fix the problem:

- ***Get invoices out promptly.*** Whatever else you do, become efficient at getting invoices out early. This is your future cash flow—the lifeblood of your business! You want to receive it as soon as possible. Start this new system NOW. Depending on your business, you can often cut out statements simply by printing at the bottom of the invoice: 'Please pay on this invoice as no statement will be sent.'

- ***Send the invoice with the goods or immediately the service is completed.*** Date the invoice from no later than the day it is sent rather than following the standard 'last day of the month' date for invoices. The earlier the invoice date, the better your chances of getting paid earlier.
- ***Change the terms for some of your customers, or for new customers.*** For example, can you ask for immediate settlement or set reduced payment terms such as 7 days or 14 days from date of invoice?
- ***Follow up promptly when invoices aren't paid by due date.*** This is critical. Be polite but firm. If you haven't the time to do this yourself, then appoint someone to do it for you.

Monitor your debtor collection days and set an improvement target each quarter. For example, can you find out the benchmark standard for your industry? If the average in your industry is 30 days, but you are taking an average of 45 days to collect outstanding debts, then there's clearly room for improvement. If your customers or clients have been taking advantage of you because of your previous laxity in invoicing, then you may need to re-educate them. Do this politely so you don't offend customers:

"Have you received our invoice, Peter? I'm just checking that you're happy with the goods/services we provided? "We've got a new invoicing system going here, because we've been a bit lax in the past. My accountant has set some tough goals for me to meet in reducing our average debt collection cycle, so if you could settle that invoice promptly I'd be most obliged."

Consider factoring. This simply means selling your outstanding invoices to a finance company. So instead of having to wait 30 days or more until an invoice is paid, you receive most of your money upfront from the finance company that then in turn collects the money from your customer. The finance company will of course charge you a commission for this service. Be aware, though, that there are pros and cons to factoring. For example, check that the finance company will not antagonise your customers with a heavy-handed approach. Talk to them first about their collection methods.

Consider offering a discount for prompt payment. If you're going to pay a fee for factoring, why not try offering a discount to your customers instead? Discounts are not a good option for low-margin businesses, but can be an option for high-margin operations. You have to work out whether the use of money gained earlier is worth the discount you're offering. NEVER give the discount if the person has missed the due date for the discount offer. (Yes, some will try this on.)

Inventory

Do you have excessive capital tied up in stock? This can occur in two ways:

- carrying high levels of items that you could obtain from suppliers at short notice
- having too many slow-moving items (and too few fast-moving items).

A quick sale?

Review regularly your stock levels, your stock turnover rates and your purchasing policies. Can you free up money by reducing stock? What about moving out of the slower-moving lines or having a quick sale of dust-collecting stock? It might pay you to reduce some items quite heavily to get some money in quickly.

Can you approach suppliers to take back any excessive stock you may have ordered? They might help you out of a temporary tight corner as a goodwill gesture if you explain you have a temporary cash flow crisis, but that you do wish to build a long-term relationship with them.

If you need additional funds to purchase more stock, make sure that you're replacing slow-moving stock with the faster selling lines.

Pre-paid expenses

This is another area you could look at. These pre-paid expenses often relate to services. For example, you might pay your insurance bill for the year all in one hit, but you could arrange to pay small monthly amounts. There might be an additional cost for doing this, but you must weigh the extra cost against the advantages of 12 small payments which your cash flow can comfortably handle versus one large annual payment. Try a similar approach with your accountant. Instead of facing a substantial bill once a year, ask if you can pay a set amount monthly.

Assets

Assets can drain significant amounts of cash out of a business. Do you really put all your assets to full use? You might be able to:

- Sell off little-used assets and hire suitable replacements when you require them.
- Lease or rent assets and equipment that depreciates rapidly such as computers and or vehicles

Customers

Don't forget your customers can be a source of business funds. Apart from debt collection improvements already discussed, try these tactics:

Here's a 'thinking outside the square' tactic. Ask some of your credit customers (start with the ones you know best) if they would be willing to use their bank credit cards for purchases from you, instead of using the account facility they have with you. For example, if they purchase say $2,500 worth of goods or services from you, they would pay for this by means of a business credit card. They still get 30 to 55 days credit before having to pay the credit card company, but you get your cash as soon as you sent in the voucher to the bank. You have to pay the (around) 5% commission, but otherwise it's almost as good as a cash transaction.

If you're starting a new business, consider establishing it on a cash only basis to keep the funds inside your business rather than locked up in Accounts Receivable.

Ask for progress payments

If you supply goods over a period of time, or if you're a service business, ask if you can invoice for progress payments. This is quite a common method of ensuring you get some cash flow during a project instead of waiting until the end of a project or delivery period to invoice—and then still waiting at least another 30 days for payment.

There's another benefit here too. If the customer turns out to be dodgy, you'll discover this quite early on instead of at the end and you can cut your losses before they mount up and perhaps drag your business down. **This tactic is therefore very suitable for tradespeople subcontracting to a developer.**

Suppliers

Finally, consider your suppliers as a possible source of funds. Ask for extended payment terms to give you the opportunity to sell the goods first before you have to pay. If the supplier won't budge, try this tactic: split the order in two and offer to pay normal credit terms (30 days) on the one half of the order and 90 days on the other half. Your suppliers will be more likely to agree to this kind of arrangement if you've paid them promptly in the past. After all, they have a vested interest in helping you succeed.

- Quantity breaks – incentivise customers to order more through quantity discounts.
- Re-order levels – Setup minimum stock levels to avoid stock outages on important lines.
- Default reorder quantity – Setup re-order quantities so the most economic order quantity is placed.
- Receive Stock – Receive items into stock so you can sell them before receiving the final bill

Take advantage of discounts

Pay accounts that give discounts on time. This is an easy one. If any suppliers offer a discount for early payment, then take it (and there is no harm in asking for a discount).

These are just suggestions and may not be suitable for your business. AV Chartered Accountants can advise you of the best strategy for your unique business needs. Feel free to contact us about ways we can help you find money in your business.

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