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Operating Your Business Takes Planning - Creative Business Planning Incorporated

The Entrepreneur's Guide to Financial Maturity ®
Managing Cash Flow

Too often I get involved when companies are facing severe cash crunches. For example, vendors have not been paid, bankers are worried and are threatening not to renew their loans, to curtail available credit or call loans. The company is operating in crisis mode. Cash flow problems are diverting the entrepreneur's attention away from the operations. Management's focus is shifted towards crisis management, ducking creditors, collecting accounts receivables and "keeping the doors open."

Being in business is an uphill battle for companies that do not have sufficient resources to fund growth. However, when a company faces pressures such as slowing sales, decreasing profit margins and/or longer collection periods for accounts receivables, appropriate actions must be taken immediately in order to conserve company assets, especially its cash.

Too often entrepreneurs fail to plan. If an entrepreneur started a business and the business has experienced growth and profitability during the first years of its existence, many entrepreneurs assume that business either growth will continue at the same pace, or there will be no growth. Many entrepreneurs fail to recognize that when their clients are hurting economically, there is a good chance they will (unless they provide services to distressed companies). Planning your way through either growth periods or economic downturns educates the entrepreneur, makes the business more agile to changing market conditions and often is the difference between thriving, surviving or closing the business.

Cash Is King:

Nobody ever went broke because they had too much cash. The single most

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important tool for building a company or saving a dying company is the skillful management of cash flow.

<u>Cash is King - Credit Is Queen:</u>

Many entrepreneurs fail to recognize that in order to build a company they must establish credit. Obtaining credit and utilizing it effectively is a method of creating stability while managing cash. Therefore, when credit is available, get it. That doesn't mean you should use your credit immediately, since <u>credit, like cash, must be managed</u>.

Try not to use your cash to purchase business assets that can be leased or financed at reasonable interest rates. If the outlook for your company or industry materially changes, financing may not be available (or if it is, it is at much higher interest rates). By depleting your cash you may be creating tomorrow's crisis, especially when business does not go as you anticipate.

Many entrepreneurs have told me that they have a profitable business, yet they are having difficulty paying their bills. They are confusing profitability with generating cash. **<u>Just because your company is profitable it does not that you will have the cash to meet your payroll or other operating expenses.</u>** Unless you are generating a positive cash flow or have access to cash to fund temporary cash flow problems, you could be out of business.

<u>Managing Cash and Credit by the Fundamentals</u>

Cash and access to credit provide financial stability, yet many entrepreneurs do not accept or act on that principle. I recognize that entrepreneurs can be impatient tracking cash flow. Small companies are particularly vulnerable to poor cash management since business owners are unlikely to employ a controller or financial officer.

As an entrepreneur, you **<u>must</u>** understand the fundamentals of managing cash flow:

- Be aware of where every dollar goes
- Practice frugality – don't spend money unless you must

- Create targets so that if you achieve your goal within a certain timeframe, you can economically justify making a major purchase you were deferring
- Make the most with your resources – stretch every dollar
- Manage by leadership – don't expect your employees to be austere with your business' resources if you're not

In order to effectively manage cash flow you, as an entrepreneur, must establish certain benchmarks and controls. Many of these benchmarks should be contained in your business plan. The business plan should contain certain financial analysis, including:

- Breakeven analysis
- Operating Budget
- Capital Expenditure Budget

Many business owners say "thank goodness, we only have to do this once." They do not understand that the business plan is a document that requires constant tracking and revision. As business conditions change so must your goals.

Periodically compare actual against budgeted results:

Analyze reasons for significant variances. Use this information to improve the company's cash management, identifying new opportunities and determining the economic viability of existing product lines. Tracking your sales and expenses against your expectations will provide some of the knowledge you will need to effectively manage your company.

Take appropriate corrective action:

If sales are lower then predicted or expenses higher than projected, understand the reason for the variance, and, if necessary, take appropriate action. Cash management, at a minimum, should be used to evaluate company/employees performance, identify unforeseen issues, track progress to any solutions provided and reduce the likelihood that the unforeseen issues becoming a crisis.

Without a proper cash management system, an entrepreneur will unknowingly defer making decisions or make the wrong decision due to a poor accounting system. Poor cash management systems cause crises.

Get appropriate Help:

Due to the complexity of operating a business and the lack of objectivity an entrepreneur may have, it is good to have the benefit of an objective party to:

- Evaluate your company's current position
- Assist in developing business policies
- Require the entrepreneur to justify certain decisions
- Cause the entrepreneur to remain focused on important goals
- Develop realistic benchmarks
- Establish accountability to others

You need the numbers to keep running your business:

The numbers are necessary whether you are operating a small business or a company with 10,000 employees. Managing by the numbers is appropriate if your company is growing, stagnating or troubled.