

Capital Corner

Did You Know?

By Jim Morphey, Vice President of Corporate Development, GE Capital, Commercial Distribution Finance

Last issue we talked about how important it is for businesses to monitor their cash flow at regular intervals, and we covered how to calculate your Cash Cycle and Cash Conversion Cycle as a way of monitoring your cash flow.

As a follow-up to those concepts, here are Ten Top Ideas to consider for improving your cash flow:

1) Think twice before financing a capital expenditure or a long-term asset with short term working capital. Not only is this very expensive, it ties up the lifeblood of your business – cash flow. If you can't find alternative long-term financing, consider leasing as an alternative to buying.

2) Consider taking advantage of terms to maximize DPO when offered. You may want to forego “early pay” cash discounts for paying your bills early, as the additional improvement in Gross Margin could be eaten up by the true cost of capital. The hidden costs of tying up working capital in inventory is usually larger than any benefit derived from the early pay cash discount, so it is important to maximize your Days Payable Outstanding (DPO) as far as possible without causing a payment penalty.

3) Consider reducing the number of brands you carry. Some may think that more variety will attract more consumers, but in reality a few core brands that meet the different needs of your consumers may actually make it easier for a customer to make a decision to purchase. In addition, by consolidating your purchasing, you maximize your importance to a few good suppliers. This helps to maximize volume

rebates, terms, advertising support etc. around your key product offerings.

4) Set short-term and long-term goals for key elements of Cash Flow, such as inventory turns and accounts receivable turns, and communicate the goals with your entire staff. Monitor monthly progress towards goals and communicate throughout your business. Motivate everybody around achieving stated goals as most everybody has potential impact on them. If you provide pay incentives to your staff, make sure they are ultimately connected to your short and long term goals.

5) Work with key suppliers on ideas to focus on targeted offerings that provide maximum profitability, and then train your sales force to sell them. Don't just focus on margin dollars but also how to generate maximum inventory turnover. Training your staff on how to move a customer to a brand you carry is an important business basic.

6) Continually work off old or obsolete inventory. Unless you're in the antique business, most of the products you sell today depreciate in value a little every month, and the total carrying costs on old

product will cost you dearly with time. Some of these costs are interest costs, increased damage, or reduced credit line availability. Remember your first loss is generally your least loss. Large amounts of old inventory is often the number-one reason for businesses to fail.

7) Limit your accounts receivable exposure. Have a strict and restrictive credit policy and minimize deviation. There are many credit sources out there, and you should use them. Unless you have the cash to invest in accounts receivable, adequate bad debt reserves, access to credit reports and the trained personnel required to manage receivables, you will be better off leaving the financing to the experts. Remember: even with mandatory large cash deposits, builder-related receivables – particularly large concentrations from a few builders – could jeopardize your very existence. Unless you are following the correct pre-notification, mechanics lien procedures don't be a bank to local builders!

8) Resist the temptation to buy your way to profitability by chasing big volume rebates. Volume rebates can be a great supplement to profitability, but they should never be the primary profit driver for your business. You'll soon forget the volume rebate you earned after you realize just how much interest you paid on slow moving inventory or tied up your credit line with the wrong mix of product. Chasing volume rebates is a little like musical chairs ... things are just fine while the music is still playing!

9) Identify aged inventory for your sales people using codes on the display floor. Most employees want to help the success of the business and will respond when called upon. Usually all they need is a little information on where the focus needs to be.

10) Develop specific goals of Return on Investment (ROI) for your business. Your business is your investment. Set a goal for your targeted ROI. You'll soon find that how you manage your cash flow – specifically the primary drivers of cash flow (Inventory, Accounts Receivable, and Accounts Payable) – have the greatest impacts on your ROI.



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