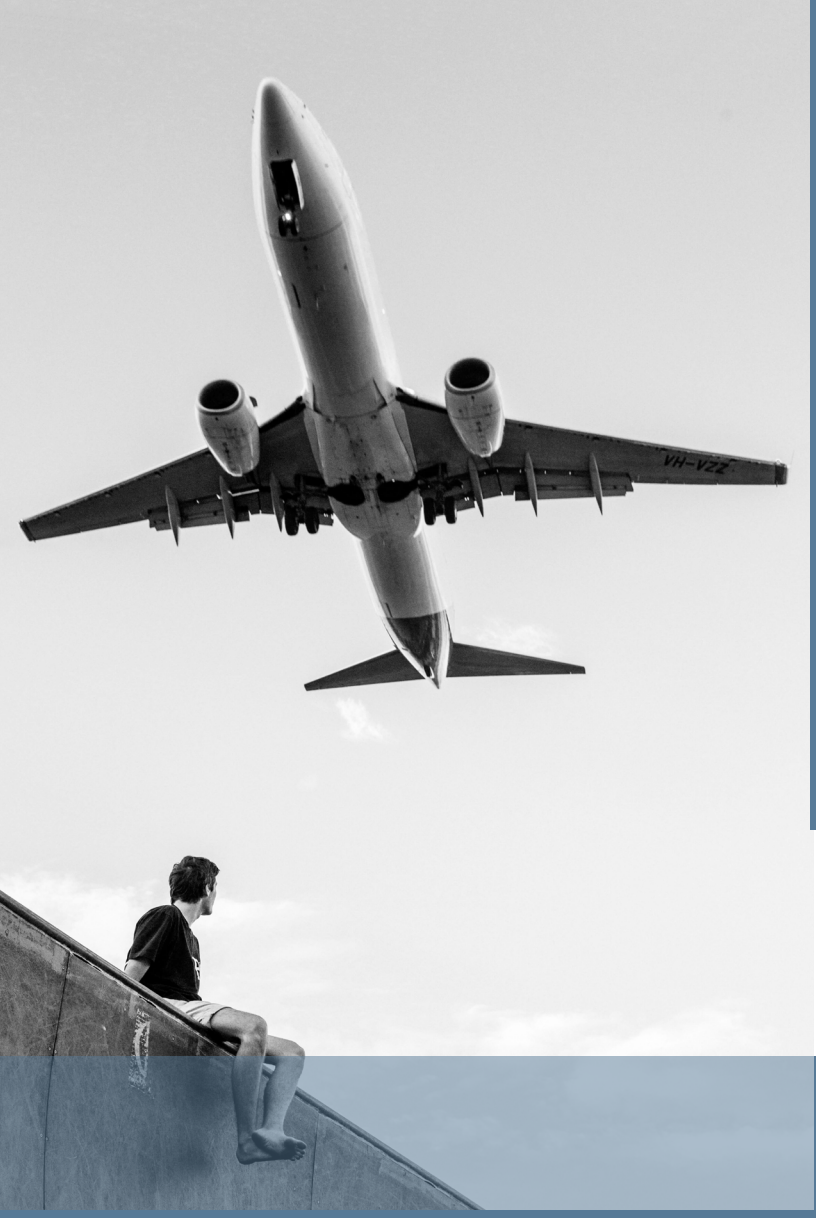


PART TIME CFO Services

LEADING YOUR BUSINESS TO A SUCCESSFUL FINANCIAL FUTURE

"Cash Is King"

Cash Flow White Paper

Part Time CFO Services LLP

Ontario, Canada
(905) 376-3025
info@parttimecfoservices.ca

www.parttimecfoservices.ca

WHY IS CASH IMPORTANT AND WHAT DOES "CASH IS KING" MEAN?

Cash is one of the most beneficial assets to have during times of financial uncertainty. "Cash is King" rings true because a strong cash flow or having access to cash allows a company more flexibility to manage their business, cover short-term operations, buy assets, acquire new facilities, or make new investments. "Cash is king" also refers to a business' ability to reduce its risks during economic downturn when demand for its products or services are low. During these times when revenue is down, elevated levels of cash make it easier for a business to pay its operating expenses and outstanding debt.

It is possible to generate lots of revenue and still not be able to pay your bills. In a situation where your customers don't pay for 30 days or longer, you may have more money going out than coming in. Plan ahead for upcoming expenses and use cash flow forecasting to be prepared for working capital requirements. Cash management is critical and poor management can lead to bankruptcy, even with a profitable business.

THERE ARE A FEW TRICKS OF THE TRADE THAT ARE ESSENTIAL FOR YOUR BUSINESS TO IMPROVE ITS CASH FLOW.

Use a spreadsheet to forecast your "real" expectations.

Build a history so you can see trends and to ensure you are covering all the cash going into and coming out of your business. Along with the balance sheet and profit and loss statement, the cash flow statement is one of the three key financial statements for a business.

Use the 80/20 rule and focus on the big dollars!

The concept of the 80/20 rule is that 80% of your money comes through 20% of your transactions or activity. Make that 20% of your business a priority. For example, do not spend an hour forecasting your phone expense and 10 mins on your payroll. Or, if you have 50 customers but 6 account for 80% of your revenue, focus on forecasting those 6 and be aware of how sales are coming in based on this. Use broad strokes on smaller clients – you don't need to spend a lot of time on the small items of your business, you just need to make an allowance for it.

Update actuals frequently. What is the impact to your future forecast?

It is best practice to keep your cash flow forecast consistently extended to 12 months out. Make sure to update it weekly with actual figures and you will create a more accurate and better cash flow forecast for your business.

Seek data from key stakeholders.

Do you have key personnel who can provide you with up-to-date information on your business stats? Ask your Accounts Receivable manager what the status is of your key customers. Who in your business makes the vendor commitments? Ask them what commitments they have made.

Complete 'sensitivity/what if' analysis of assumptions.

The reality is every forecast is wrong. No one can accurately predict the future, so run different scenarios from both a very pessimistic view and an optimistic view. Consider what the implications would be on your need for cash

Be objective!

Do not force your assumptions to achieve an overall goal. If you are trying to create a cashflow using your bias to generate a number you want, you are not going to have a good cash flow forecast. Ignoring what the reality will be will not help in creating an accurate forecast.

TOP 7 PITFALLS THAT WILL HURT YOUR CASH POSITION

1 Excessive pre-buying to achieve volume discounts

The two risks with this tactic are 1. having cash tied up and 2. obsolescence. By using cash to purchase extra inventory, your working capital is artificially increased and these dollars are unavailable elsewhere in your business. Additionally, there is a bigger risk in the obsolescence of that inventory due to factors such as technological and market changes that can make a product insignificant and subsequently difficult to sell or sold at a loss.

2 Large shareholder withdrawals/salaries

Ensure your business is healthy and sustainable and that you have put the business' financial needs ahead of your own. Prematurely extracting profits from the business to fund a lifestyle it cannot support, can lead to its downfall. Wealth and income will be there in the future.

3 Long term financial payment commitments

Understand the future cash flow implications of taking on debt. Debt is attained easily but once acquired, you have a future obligation to make monthly/weekly payments. It is essential to keep the right balance of future loan payments vs. future cash flow/profits from the business.

4 Too many bank accounts and credit cards

As the number of bank and credit cards increase, so does managing these accounts and requiring payment and planning. Fewer accounts make it easier to stay on top of your cash flow activities.

5 Using customer deposits to pay for other discretionary expenditures

Having the discipline to use customer deposits to put towards expenditures related to that customer's projects will keep your future cash flows in line. Just because you have a large balance in your account does not mean you have funds available to purchase that new piece of equipment or other items. Having a cash flow planning model will give you the visibility to ensure that cash is there for all expenditures when required.

6 Giving credit to customers without any review for credit worthiness

'Credit is Earned'. A sound credit review process/policy can significantly reduce your risk of non-collection. Just because the customer can issue a purchase order does not mean they can pay for your product/service. Do your due-diligence to ensure they can pay you when invoices come due. Any sale that comes with bad debt is a sale that you do not want to have.

7 No forward-looking tax planning/strategy

Work with your finance team and plan that there is no lag to payments for income tax and retail sales tax. The penalties and interest charges from government agencies for non-compliance can add significant stress. Keeping in good statue with your government commitments will keep them "out of your business." The last thing you want to do is focus your time on dealing with government agencies over a default payment – you want to have that time to focus on your company.

SOURCES OF FINANCING



Profits

As profits increase over time, use this cash to fund your requirements, reducing the need for third-party loans. This is usually the preferred way to finance your business. There is no cost with this option, however there are opportunity costs for shareholders (dividends) and staff (bonuses).

Personal Savings and Wealth

The easiest lender that understands your business well and is the most confident in your business is you, the owner. It is the quickest way to get funds in your business when required. To avoid putting yourself at financial risk, you need to be able to step back and review the business situation. Ensure that you are not putting your funds into a business that might not be performing.

Banks and Credit Unions

Traditional financing is your cheapest cost of third-party money. Funding from these sources does come with a great deal of requirements from security to formal financial reporting and personal guarantees.

Family and Friends

Often this group supports early-stage companies and is all based on your personal relationship. You must weigh the benefits of getting money from them against the relationship you have outside the business.

Credit Cards

This is a last resort as the interest rates and fees are quite high. However, in early-stage companies, this is often used due to the inability of getting financing from other sources.

Private Investors (Venture and Angel Capital)

This type of funding falls into 2 categories: in the form of a loan and through capital injection. A loan can incur higher interest rates to reflect the risk investors are taking. However, this type of lending requires less security. If investors are participating through a capital injection, they are looking for healthy returns to reflect the risk they are taking from entering a business at this stage. Look for partners that have strategic relationships that you currently do not have that can make a positive impact on future results of your business.

Government Agencies and Programs (BDC, CFDCs, OCE, IRAP, SRED, EDC, etc.)

Do your due diligence to find the right programs and partners in this space. Do not make the mistake of chasing every grant and subsidy or you will lose focus on your business.

Accounts Receivables Factoring

Once again, this is a high-rate cost function to create liquidity. It is, however, useful and more economical when bank loans have been exhausted. This is one of your last resorts of cash liquidity, but can be powerful and create significant liquidity depending on your level of A/R. Make sure you understand all costs and fees related to this service offering.

Customers

Using a combination of 1. obtaining customer deposits, 2. reducing your terms of payment and 3. improving your accounts receivable collection on already established terms, will increase your cash flow and reduce the need for financing.

Vendors

Work to extend your payment terms with vendors and eliminate or reduce the deposits required.