

**Financial Finesse Series
Article 2 – Cash Matters**

You've heard the saying, "*you've got to spend money to make money*". While that may be true, when you're a small business owner that can be easier said than done. Is your sales volume growing but you feel stressed that money is still going out of your chequing account faster than it is coming in? In this article we will discuss some of the reasons why that may be happening and what you can do to deal with the challenge of the cash crunch.

If you find yourself struggling to deal with the growth of your business, you can identify with Karen Murphy, owner of Express Gift Baskets in Kelowna. Over the past 10 years, her company has experienced tremendous growth. "I started Express Gift Baskets in 1997 with a \$10,000 personal line of credit. I soon realized that because my business was inventory-based, I could quickly become under-financed as orders became larger. If I wanted to go after bigger accounts where I would require stock before payment of orders, I was going to have to make a decision to take on some long term debt."

Trickling sales don't tend to produce a lot of income. But now that things are moving, shouldn't the cash flow situation be different? This is what you've been waiting for. Why are you still struggling to find cash? The answer to those questions is that there is an inevitable lag between what it costs to generate business capacity and being in a position to reap its rewards.

Some might argue that, with sales flowing steadily through the door, the financial strain of business growth is a good problem to have. Difficulties arise, however, in managing the costs that must be incurred in order to meet the demand. You need the cash to fund production to meet the needs of a growing customer base, so how can you accomplish that?

Quite often, cash flow crunches mean taking on debt. That was the case for Karen Murphy who recalls her first expansion, "After a year, we took on about five times the original start-up money required. That was enough to carry substantially more inventory, allow for better equipment and also to hire an assistant."

"By the end of the fifth year, we needed to expand again to a larger facility. We now had more business all year round and contracts large enough during the busier time to warrant more staff. We then also required more inventory and more equipment. Our last expansion was the largest and was now about ten times our original money invested."

Acquiring business debt can be unimaginably frightening. It's one thing to take out a loan for a car or a new piece of furniture where you can touch it, feel it, or put it in your living room. A business, on the other hand, is more intangible – and more risky. Then there's always the chance that the business might fail. Do you really want to put your hard-earned assets on the line?

Why are women often so reluctant to take on business debt? It may be that we are uneasy taking a gamble on ourselves, particularly when there are others, like children or an elderly parent, who rely on us financially. Regardless of why we fear debt, to grow a business, you're going to need cash. Underfinancing often shows itself in inconsistent service, an inability to fill large and potentially lucrative orders and even poor morale.

Where will you get the financing to grow your business? There's the traditional term loan, and then there is what amounts to supplier loans, or credit. Supplier credit (ie managing your payables) can be a key source of liquidity when nothing else is available. Using this form of credit requires that you stay on top of who you owe money to, and paying those bills at the last possible moment, so you keep your funds longer. You need to resist the temptation to pay those bills as soon as they come through the door. Hold on to them for the penalty-free period, and you've acquired for yourself an interest-free loan for usually up to 30 days.

On the other hand, when *you* are the supplier, the quicker you collect on your outstanding accounts the better. Small businesses typically can't afford to finance their customers for very long and if you've ever been in the position of having to chase down a delinquent client, you know it's not fun.

Following through on collections can be an intimidating task for many women entrepreneurs. We worry about offending our customers by asking them to pay their bills. We don't want to appear rude, or have them not like us. The next time this sounds like you, ask yourself whether you feel flush enough to extend an unlimited, interest-free loan to the customer who falls behind on payment. Here are a few simple strategies you can use to help make sure you are paid on a timely basis:

1. Require that new customers submit a credit application and actually check their credit references or, alternatively, require that new customers pay you in cash;
2. Do not continue to sell to customers who repeatedly fail to pay you on time. Remember, a sale is not complete until the money is in your hands;
3. Apply strict penalties on late payments, including surcharges and/or loss of credit privileges;
4. Contact – preferably call - customers immediately for payment of overdue accounts.

Growth in our business and delinquent customers are not the only reasons cash flow can come under pressure. A new company often has money tied up in inventory and other, non-liquid assets like equipment and vehicles. It's important in the early stages of business to know the difference between what's necessary and what's a 'nice to have'. If you're going to tie up your money, make sure it's for the things that will allow you to secure customers and meet their needs in the short-term.

One of the best ways to ensure that you have enough cash to keep your business running is to prepare a cash flow statement. This is a statement that both forecasts and tracks money flowing into and out of the business *as it changes hands*. A cash flow statement does not reflect sales when they are confirmed, but rather when payment is received. Similarly, it does not reflect costs when they are incurred but rather when payment is made.

The mistake many business owners make in forecasting their financial position is bundling inventory and/or production costs with related revenues in neat little monthly packages. Essentially, they ballpark their sales per month, determine how much the sold products will cost them to produce, and then assume that the net of those two figures will fall into their hands every month in the way of cash. Not so.

Take Diana Alexander, owner of Elite Beauty Group Inc. in Terrace. When Diana decided to add a new service to her salon and didn't anticipate the considerable lag she would experience between the investment to set up the service and the sales needed to cover its costs. "The bills," Diana recalls, "came right away but we hadn't promoted the new service enough to get the sales needed to cover them. For three months, the loss was substantial."

Diana now uses cash flow projections to guide her business. "They are key to helping me stay on track financially," she says. "Since the buck stops with me, they are like my supervisor. Based

on the numbers on the cash flow, I know what I am allowed to spend and what I am expected to bring in each month. Watching over cash flow motivates me to stay on track so I can succeed.”

The benefit of developing realistic cash flow projections and budget is that it can save you the heartache of fatal cash deficits. You can plan ahead to cover shortfalls, and resist the temptation to spend every cent you collect as it comes through the door. That makes for a healthy business and takes a lot of the stress out of financial management. With stress levels down, it also makes for a healthier *you*.

Women's Enterprise Centre is the go-to place for BC women business owners for business loans, skills training, business advisory services, resources, publications and referrals. Call us at 1.800.643.7014 or email info@womensenterprise.ca from anywhere in BC.