Solving Cash Flow Challenges

Creating cash flow: your guide to navigating today's cash flow challenges through the learnings of Australian SMEs.

ScotPac
Business Finance

Call **1300 145 344** or
Visit **ScotPac.com.au**

Contents

ScotPac
Business Finance

A barrier to growth

For an agency at any stage of its life cycle, having steady and predictable access to cash is vital.

When cash is flowing, the business has a positive pool of working capital to fund its operations. Being able to improve the rate of cash flow increases the working capital available, and the ability to meet financial commitments as they fall due.

With recent times being challenging, some businesses have seen a large downturn, diminishing available working capital and straining cash flow. Mounting pressure from creditors and other financial commitments has left these businesses in a tight spot.

On the other hand, rapid sales growth can also impact cash flow, and some industries have seen a surge in demand. While such demand would normally be welcome, when it comes at once, it can expose a business to the risk of overtrading. As businesses experience rapid growth, they may also seek more staff, equipment, inventory and resources to keep up with demand and this investment requires additional working capital.

Every successful business has its own unique features, yet effective cash flow management is a common thread. Many profitable businesses experience peaks and troughs in their cash flow and need an injection of working capital to help keep them moving.

In this guide, we will provide you with important tips and techniques for overcoming your cash flow challenges in order to help drive growth.

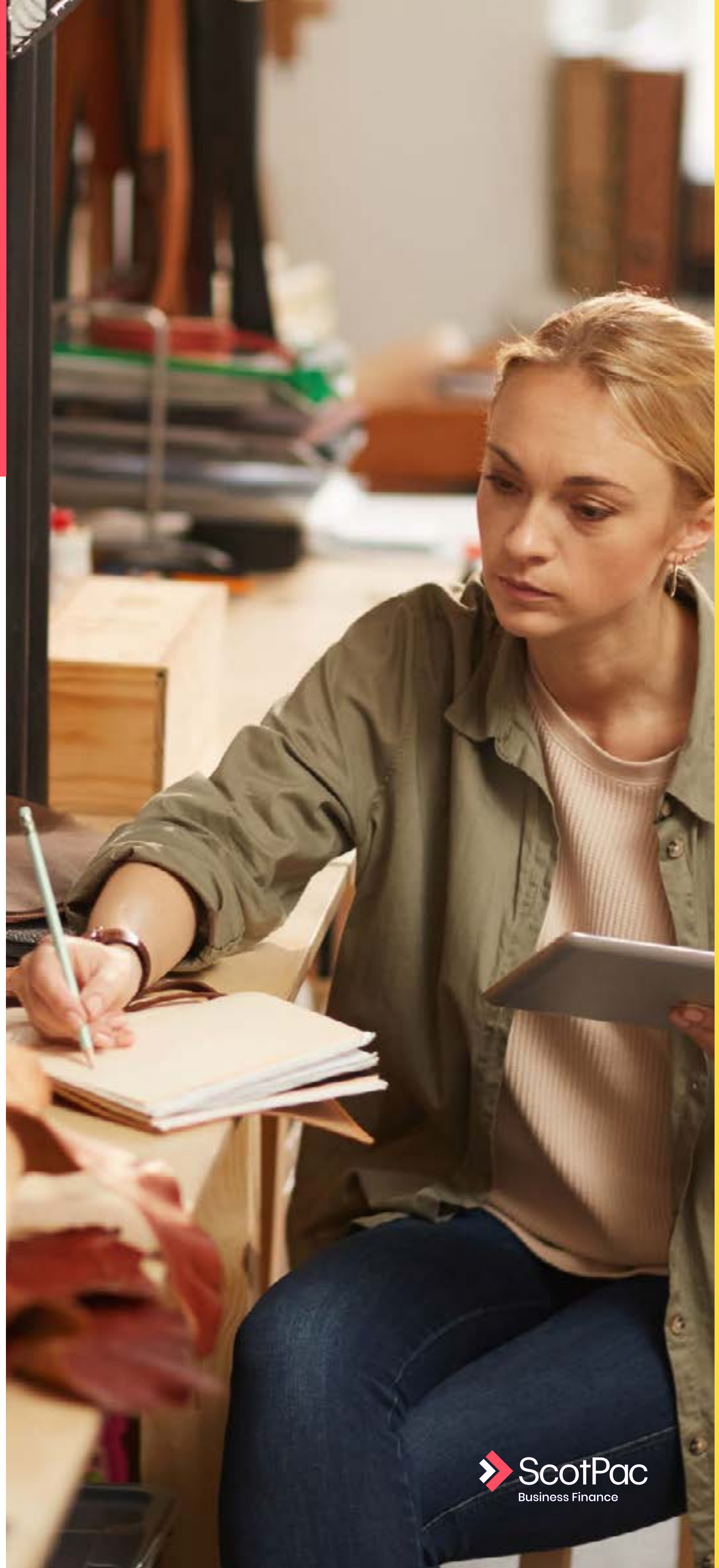
ScotPac
Business Finance

A cash flow action plan: Identify the causes and their effects

If your agency has experienced cash flow issues recently, you're certainly not alone. In fact, the recent ScotPac SME Growth Index showed that SMEs are three times more likely to use personal finance facilities like credit cards to manage rising business costs.

Here are some of the top issues identified by business owners and directors

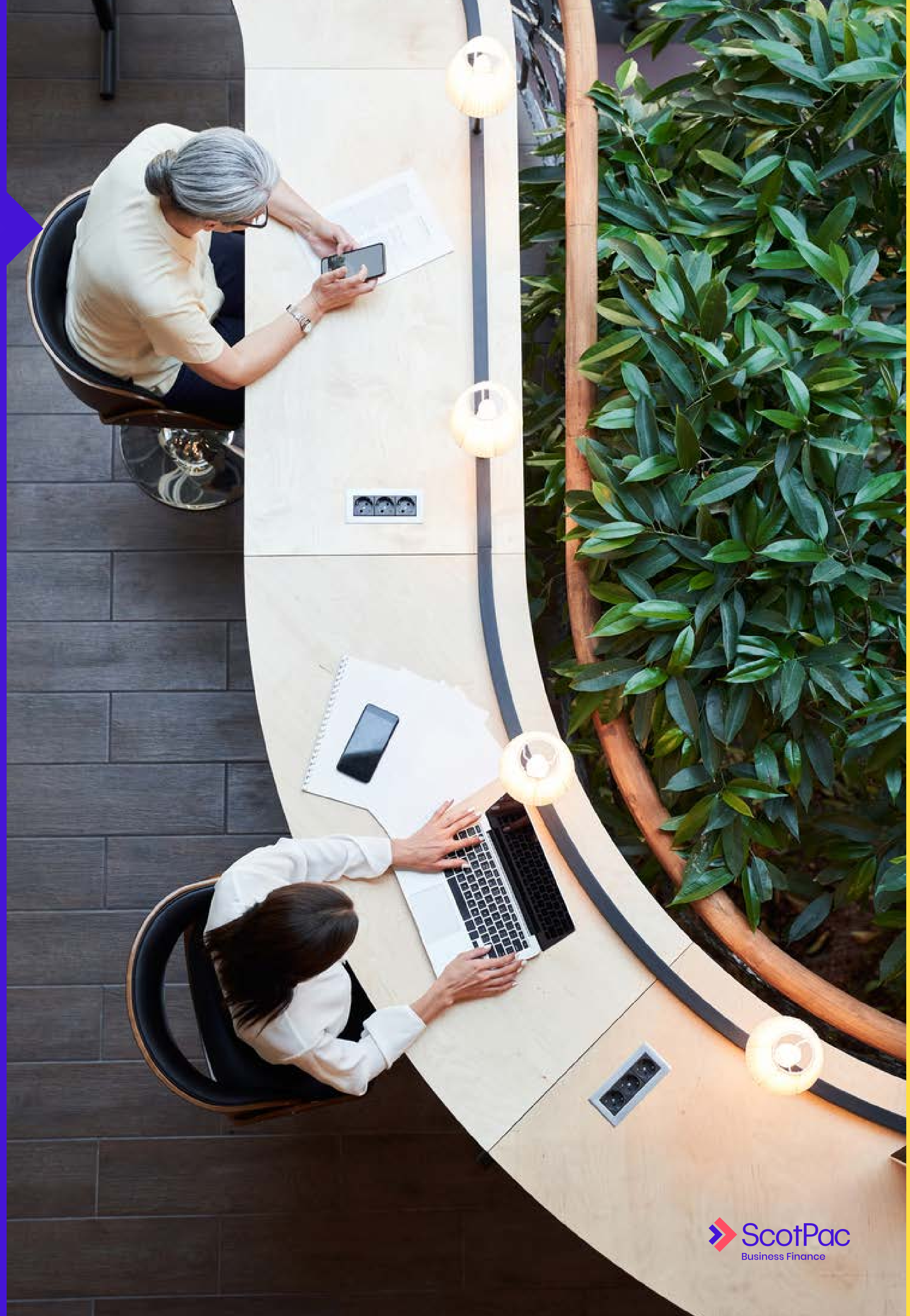
Cause	Effect
Clients paying late Not getting paid on time can be very damaging to a small agency. It can seriously affect your ability to meet your own expenses and maintain your working capital.	**Unable to take on new work** A lack of cash flow can also impede your ability to take on new work. Fulfilling orders requires working capital to pay for wages and all the other costs of running your business.
Clients reducing payment time When a client insists on reduced payment terms, it can have a major impact on your cash reserves; particularly if you need the income to pay your on-hire workers.	**Difficulty meeting tax payments** Typically, your tax obligations can be the first to be stretched when your cash flow is tight. However, at some stage the ATO will be looking to be paid the tax debts which are due.
Bad debts When an account isn't paid, you're not only missing out on anticipated revenue, but you've already worn the cost of the time, wages, and other expenses invested in the work you've completed.	**Poor cash flow management** Significant amounts of cash can be locked up in receivables, impacting the ability to pay staff and overheads.



8 tips for overcoming common hurdles

Understanding cash flow problems is the key to managing them.

On the following pages, is a checklist that can help your agency deal with some of the most common issues faced by small to medium sized agencies.



Tip 1

Invoice on time, and consider deposits and discounts

When it comes to cash flow, being punctual with your invoices is essential. Make sure you invoice as soon as the job is done.

The earlier you invoice, the sooner your payment terms kick in and your clients are required to pay.

You could also consider asking for a deposit upfront, or a percentage of the job's value. This can be a reasonable request and something many businesses do. A 10% or 20% deposit on each order can help meet the costs of hiring additional labour or purchasing from your supplier.

Alternatively, if a client has been loyal and their agency is ongoing, then it might be time to reward them with a discount for early payment. However, be selective when making this offer. It's your regular paying client who should get the discount.

Cash flow handy tip

Make sure your invoice is set out clearly and is easy to understand for your customers, so there isn't any delay in payment simply because there were questions regarding the invoice.

Ensure you have quoted the customer's purchase order number, itemised charges, clearly set out payment terms and ways to pay.

Also be sure you are addressing and sending the invoice to the person who will be paying this to ensure it doesn't go astray.

Cash flow handy tip

Consider adding a penalty for late payment of invoices, with the size of the penalty determined by how long the invoice is overdue by.

So, if it's one month late, consider applying a 5% penalty and explain this is necessary to help cover the additional cost of collection. If it's two months late, apply a 10% penalty. Clearly communicate any potential penalties at the time of invoicing.

Tip 2

Proactively deal with potential late payers

If a client is tardy with their payments, take action before payment is due, no harm sending a polite reminder that your invoice is due to be paid next week. If a client is known to query invoices or ask for dockets or timesheets, be proactive and find out early before payment is due, queries and disputes are resolved, and you are paid on time.

Having a good credit controller and keeping on top of your clients for payment is worth its weight in gold.

It's an old cliché, however those who shout loudest get paid first. chasing the payment of overdue invoices is critical to maintaining positive cash flow.

It's also important not to be too generous with your payment terms, whilst operating within industry standards. If you are unsure of a new customer's credit worthiness, take out a reference from their other suppliers or do a credit check. Alternatively, start them on a small limit with short terms, such as 14 days, until a track record is established.

Tip 3

Offer customers more ways to pay

By making it easy for your clients to pay you, you'll give them fewer excuses for not paying. If you don't offer payment by credit card or BPay or 'buy now, pay later' options, then perhaps you could consider these.

Also, offering PayPal as an option if you trade online may also boost your chances of immediate payment.

It's important to ask these questions when choosing a payment method:

- How do your clients prefer to pay for your services?
- Is cash-only payment going to harm your business?
- Will you have to follow up with clients for payment of your services?
- What costs are involved in each payment method?

Cash flow handy tip

The most common payment method for goods and services is through electronic credit and debit cards. It can be worth offering your clients these payment facilities.

Cash flow handy tip

If you're chasing an outstanding debt, always call first rather than email.

You can ask about their needs and preferences and even suggest other products or services they might like. You might also get important feedback on your business.

Cash flow handy tip

If you can't pay your tax on time, you can proactively contact the ATO to enquire about setting up a payment plan.

You will still need to lodge your activity statements and tax returns on time, but could avoid the FLT penalty, as long as you're aware of your obligations and doing your best to meet them.

Tip 4

Maintain strong relationships with customers and suppliers

To secure payments, a positive relationship and communication means a great deal.

If you are struggling to make a supplier payment, let them know and negotiate extra time to pay. Similarly, encourage your own clients to do the same thing.

Rather than speaking directly with the accounts department, get in touch with your representative at the customer or supplier organisation.

Tip 5

Stay on top of your tax position

Having to make a substantial tax payment can seriously dampen your cash flow and create all sorts of stress for a business. When it comes to tax, ensure that you file your tax documents on time to avoid being hit with a failure to lodge on time (FLT) penalty, by creating a calendar that will remind you of important tax schedules and payments.

Tip 6

Regularly review your funding arrangements

When you simply don't have cash reserves, there are plenty of funding options to choose from. However, it's important to make sure you choose the right option for your business. If you already have funding arrangements in place, assess whether they are still suitable for your current cash flow requirements.

If they aren't, speak to your lender about different alternatives or aim for more favourable terms. Reducing loan repayments can simply be a matter ofcalling your bank and asking for a longer term to repay.

Think about arranging a line of credit with your bank before you fall short. Banks are far more receptive to helping you out if you ask well before any cash flow problems arise.

Cash flow handy tip

If you are going to use credit cards, its best to pay them off monthly to avoid high interest charges. As an alternative, talk to your lender or adviser about other, more cost-effective lending options.

Tip 7

Produce regular cash flows and create a budget

Cash flow forecasting and budgeting is essential in allowing you to identify periods when spending is high and when cash is likely to become scarce.

A monthly budget forecast should tell you who you need to pay, when payments are due and what your likely cash outflows and final position will be.

A cash flow projection should include all the cash that you expect to receive in the period. This includes sales revenue, loans received, investment earnings and other sources of income. Be sure to include all cash outflows, such as wages, loan repayments, taxes, supplier costs, insurance and other expenses.

This exercise is vital to help you assess your working capital and make plans now to counter a cash flow shortage.

Cash flow handy tip

Pay only what you need to over a tight period. While wages are essential, defer what you can and take advantage of your supplier's or creditor's payment terms to pay on the last day when invoices are due.

Tip 8

Consider working capital finance

Working capital finance is a line of credit linked to your outstanding accounts receivable. If you do need help with your working capital to overcome temporary cash shortages or to meet ongoing cash requirements, then this form of finance will enable you to turn your outstanding invoices into cash rather than waiting for payment on the due date or later.

An invoice financier may pay up to 90% of your invoice value within 24 hours after it has been issued, and pays you the balance, less a small fee, after they have collected payment from your customer. Unlike a traditional bank overdraft, there is generally no need for real estate security.

Cash flow handy tip

Research the alternative lenders and their lending options.

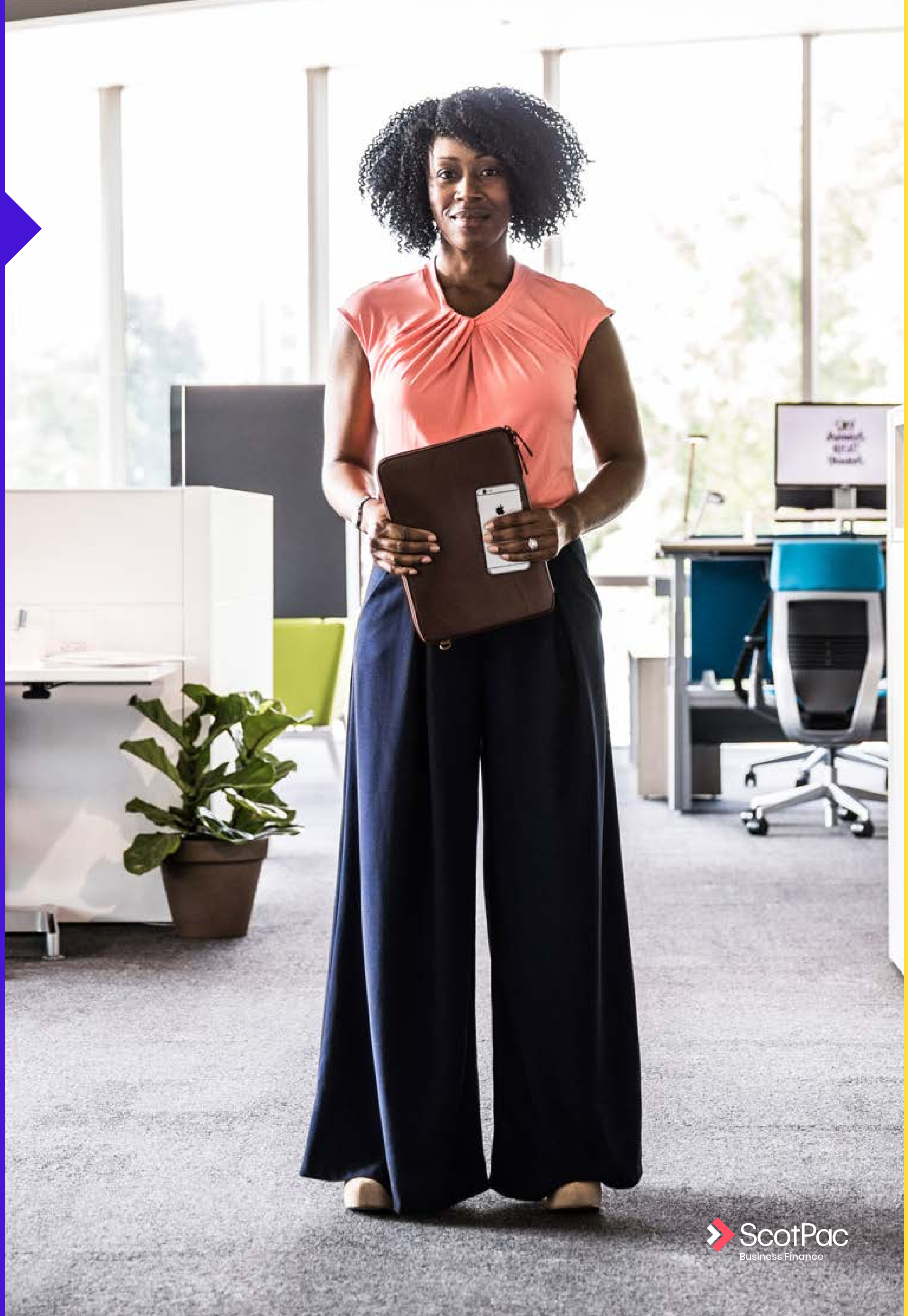
You should talk to your business adviser and make sure you assess all the elements of a financing proposal to make sure it is the best fit for your business.

How much working capital do you need?

Working capital is the difference between a company's current assets and current liabilities.

It is a measure of whether a company has enough liquid assets to pay its bills that will fall due within one year.

Current assets, such as cash and accounts receivable, are resources a company holds. Current liabilities are the amount of money a company owes to others, such as accounts payable and debts that are due for payment within a year.



Section 3: How much working capital do you need?

Working capital = current assets – current liabilities

This working capital formula tells us what a business's short-term, liquid assets are after deducting their short-term liabilities. It is a measure of a company's short-term liquidity and knowing this is important for managing cash flow.

A significant amount of working capital indicates healthy levels of liquidity. Minimal or negative levels of working capital indicate low levels of financial capacity — and this is what you want to avoid in keeping your business alive and profitable.

To the right is an example balance sheet used to calculate working capital.

Current Assets	
Cash	$50,000
Accounts receivable	$30,000
Inventories	$40,000
Current Assets	**$120,000**
Current Liabilities	
Accounts payable	$25,000
Short-term borrowings	$10,000
Accrued liabilities	$10,000
Current Liabilities	**$45,000**
Working Capital	**$75,000**

Working capital requirement

Another way to calculate your working capital requirement is to use the following formula.

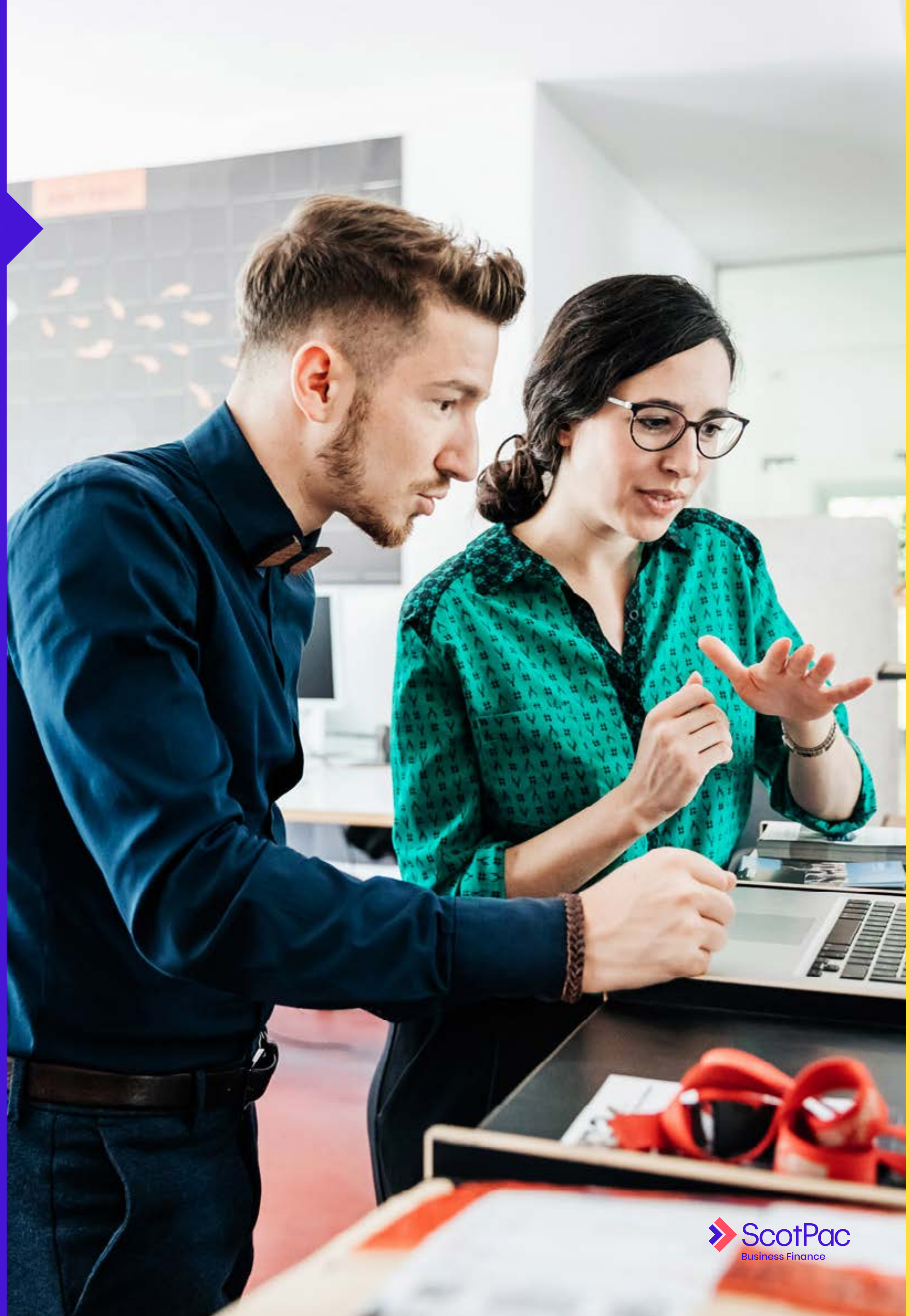
Cost of goods sold (COGS) measures the direct costs of producing the goods sold by a company.

The 45 days is the debtor days figure: debtor days is calculated as the value of your receivables divided by your total annual credit sales, multiplied by 365.

The business has: $10,000,000 turnover	
COGS	$6,000,000
Overheads	$3,000,000
Current Assets	**$9,000,000**
	/ 365 days
Per day 45 days	**$24,658**
Working Capital (45 days)	**$1,109,610**

ScotPac Business Finance

4 tips for smarter cash flow management



Tip 1

Invoice in instalments

Instalment payments can help to alleviate cash shortages. Like asking for a deposit, it means invoicing in stages, rather than waiting until an entire project is complete. The construction industry is good at doing this, and it can pay to take a leaf out of their book.

Depending on how your accounting system works, you could issue two or more invoices on the same day with different due dates. Alternatively, you could issue a single invoice with each instalment listed as a separate line item. Either way, by not waiting until the end of a project to invoice, you'll be getting cash sooner.

Tip 2

Prepare a rolling quarterly cash flow forecast

As you are forecasting three months ahead, you will find it easier to immediately recognise peaks and troughs and identify any warning signs.

Tip 3

Invest in good accounting software and pay as you go

Software as a Service (SaaS) is the way to go these days. The beauty of SaaS is that you pay for use of your accounting software in instalments and you automatically get upgrades. You don't need to pay out a lump sum for software that might date quickly. Research which software is best for your agency and modernise your software if you need to avoid time-consuming manual invoicing.

Tip 4

Do your debtor due diligence

Conducting credit searches on new customers, as well as periodic checks on your key customers, is an excellent way to ensure the cash keeps growing. Act on any signals you might be picking up about their credit worthiness and keep across their payment habits, as bad debt can be one of the most destabilising events for your agency's security and success. It might be worth considering Trade Credit Insurance as a way of protecting your agency against this risk.

ScotPac
Business Finance

A financial solution to get cash flowing

There are a number of working capital and cash flow finance tools now available to businesses.

These range from the traditional overdraft to merchant cash advances, P2P loans, marketplace lenders, SaaS cash flow management tools, unsecured lines of credit and online business loans.

One solution which is growing in popularity globally is receivables finance (also known as invoice finance) which essentially involves the selling of a business' accounts receivable in exchange for a cash advance.

This means the cash from a credit sale can be accessed and put back to work quickly to pay down creditors or fund new sales.

Invoice finance does not typically require property security and be used on either a short or long term basis.

ScotPac Business Finance

What are the benefits?

It is a powerful standalone business finance facility, which helps because:

- As your agency grows, the facility grows with it.
- Unlike a traditional bank overdraft, there is generally no need for real estate security (e.g. your home)
- It is a standalone facility that can sit alongside other agency borrowings (such as overdrafts, term loans, and asset finance).
- It helps you grow your business and increase purchasing power through improved cash flow.
- Speed of approval and funding, benefits of a close relationship, flexibility, leverage your client's credit rating not yours.
- Helps strengthen client relationships through prompt payment.

How invoice finance works

Once you have secured invoice finance, drawing upon it is easy:

- Upload invoice: You invoice your customers directly and upload the invoice to your financier at the same time.
- 24 hour approval: The invoice financier will pay up to 90% of the value of approved invoices, less fees.
- Cash advancement: The remaining 10% becomes available to you when the invoice is paid in full.

With platforms like ScotPac Cash Connector this process can become even easier with direct integrations into your cloud accounting.

Find out more at:
scotpac.com.au/our-solutions/invoice-finance/

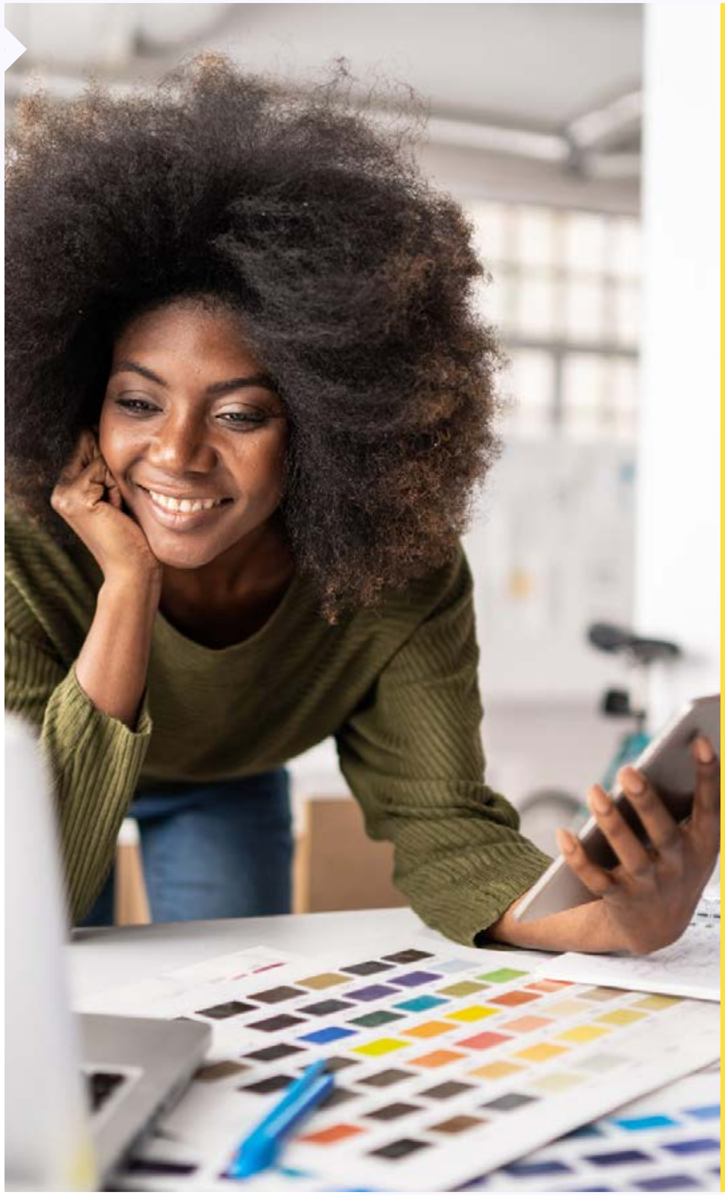
Find out if cash flow finance is right for your agency

Whether you are looking to expand, boost working capital or improve your day-to-day cash flow, ScotPac has a range of invoice, trade and asset finance facilities and business loans that can help.

Call **1300 177 485**:
Speak to one of our experts on funding.

Email us: **enquiries@scotpac.com.au**

Get started: Use our handy **Product Selector Tool** to see what option is right for you.



About us

Simply put, our aim is to give business owners a better chance of success. ScotPac is committed to supporting businesses across Australia and New Zealand.

We strive to provide the most comprehensive range of working capital solutions to meet all types of business needs. Our solutions are tailored towards improving cash flow to generate the funds that businesses need to realise their goals.

Find out more about what ScotPac can offer your business.

Call **1300 177 485**
Visit **ScotPac.com.au**

Follow ScotPac on social

Office Locations

Adelaide
Auckland
Brisbane
Guangzhou
Melbourne
Perth
Sydney

ScotPac
Business Finance