

## How to keep your cash flow healthy

*Seeking additional funding from banks or investors isn't the only thing you can do to improve cash flow in a flagging economy, says certified accountant Anita Brook.*



Whenever a recession hits, one of the worst affected groups is small business owners. With budgets restricted, people not only tend to buy less, but they also tend to take longer to pay, putting a squeeze on suppliers' cash flow. And, of course, as businesses wait to be paid, they are forced to delay payment to their own suppliers, so the impact of the economic downturn becomes magnified.

If you find your business in such a situation and are unable to borrow additional funds, it can be easy to get disheartened, but there are other ways to improve your cash flow and ride the recession out.

### **Budget carefully**

The key to keeping cash flow healthy is careful budgeting. This means not only projecting income and expenditure at the start of the year, but also tracking transactions on a daily or weekly basis to ensure you remain in control of your finances and avoid overspending.

You should avoid building up large bills on account wherever possible as this will only delay the inevitable and have a worse impact on your cash flow further down the road. Plan and budget in advance for all large purchases and create a petty cash pot for sundries. Replenish the pot with a set amount each month and make a rule that if the pot is empty, staff must wait until the following month rather than dipping into other funds.

### **Limit risk**

For many small businesses, the failure of a major client who declares bankruptcy with invoices outstanding could spell the end, so it is worth taking time to research a client's ability to pay before agreeing to fulfil an order. There are number of agencies that can provide information on business credit scores, while some business bank accounts include this service for free.

If you are particularly concerned about exposure to bad debt, it may be worth considering speaking to your insurance broker about credit insurance. This insures business against the losses incurred by bad debt and usually covers credit control and legal costs as part of your premium. However, insurers will not underwrite clients with poor credit histories, so if you are considering credit insurance, you should first weigh up the potential savings against the expense of putting a policy in place.

### **Get paid faster**

Many businesses keep things simple by invoicing all of their clients at the end of the month, but if cash flow is poor, billing more regularly, or even immediately after an order is fulfilled, can be an

effective way to free up funds.

If you are providing an annual service, you could also consider offering a payment plan which spreads the cost across throughout the year and helps both your business and your clients budget more effectively. This approach also reduces the potential loss should the client go bust later in the year.

### **Encourage prompt payment**

If you are struggling to bridge the gap between billing and receiving funds, you could consider offering a discount for early settlement. This can be an effective way to improve cash flow, but the benefits of accessing the funds early should be weighed against the percentage you will lose as a result of the discount.

If late payments are becoming an issue, set up flags on your calendar or within your bookkeeping software to remind you to chase payments immediately when they become overdue. Many companies are simply deciding to hold back on making a payment until they are chased by suppliers, so a prompt phone call can make a world of difference.

### **Release funds via a third party**

For businesses who have reached the point where they simply do not have the cash to continue trading, releasing funds via a third party can be a life preserver, but can prove very expensive.

Invoice factoring involves selling an invoice to a third party for a percentage of the true value (often 80%). This typically allows businesses to access funds within 48 hours, well before the invoice becomes outstanding. Similarly, purchase order financing allows you to secure funding from a third party against a purchase order. Again, however, there is a fee involved, so this option should generally only be considered if you are in a position where you would otherwise be unable to fulfil the order.

Ultimately, keeping cash flow healthy is always going to be a challenge for the majority of small enterprises in a recession, but the businesses that survive the economic downturn will be those that keep a close handle on budgeting and take every step possible to limit exposure to bad debt and encourage prompt payment for services and goods outstanding.

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