

Managing Money: Cash Flow

“Whoever can be trusted with very little can also be trusted with much, and whoever is dishonest with very little will also be dishonest with much”

Managing Cash Flow is all about managing the timing of money coming in and money going out. To help understand this, let's look at the basic ingredients and review some definitions to ensure we understand the essential building blocks for managing cash flow.

Basic Ingredients:

1. Good Planning
2. Good Record Keeping & Accounting
3. Good Management

How does Cash flow work?

Cash flow is the movement of cash into or out of a business over a specific time horizon. It has to do with having enough cash on hand to fund the expenses of the business at the time that the cash is needed.

- It is possible for a business to be profitable but to go bankrupt because of the timing of when cash goes out and when cash comes in
- Planning & saving are essential ingredients to managing cash flow
- Equally essential is knowing when expenses are due and when income will be collected
 - Part of this will be an analysis of which expenses can be moved further out and how you can bring the income sooner.
 - So enquiring about credit terms for paying your suppliers can help
 - Aiming to sell ratably (i.e. spread out your sales so that you sell an equal amount of products each day) rather than selling on only one day a week. This can also assist to smooth out the flow of cash through your business
 - You could also use your marketing mix to attract customers to pay a deposit or to pay 50% up front but this may require you to give them a price discount. Though you may reduce your profit at least you won't go bankrupt!

Example 1

You have R500 and need to work out whether you have sufficient cash flow to make it through the week. Your income and expenses plan is as follows:

Details	Amount
Cash on Hand	500
Salaries & Wages	250
Purchase wood for chairs	200
Purchase paint, nails & glue	75
Allowance for unplanned expenses	60
Payment of rent	150
Sale of products	900
Profit for the week	665

This budget forecast shows that from the R500 of cash on hand, my business will make R665 in profit after all income and expenses have been accounted for.

BUT – Now let's look at this from a cash flow perspective where we add to this the timing of the Expenses and the Income:

Day	Details	Amount	Cash Flow Analysis
Friday	Cash on Hand	500	500
Saturday	Salaries & Wages	250	250
Monday	Purchase wood for chairs	200	50
	Purchase paint, nails & glue	75	-25
Tuesday	Allowance for unplanned expenses	60	-85
Wednesday	Payment of rent	150	-235
Thursday	Sale of products	900	665
Friday	Profit for the week	665	665

From the cash on hand, you can pay the Salaries & Wages on Saturday. However, before you are able to pay for the wood on Monday, which costs R200, you will go bankrupt - even though the income that you will get on Thursday is sufficient to cover all of your expenses for the week.

*** As you can see this timing can't work!**

So what options are there?

1. You need cash on hand of at least R735 in order to make it through the week
2. Look for expenses that can be moved later (such as the rent or the salaries & wages)
3. Look for ways in which to shorten or quicken the business cycle
 - a. Perhaps you can make and sell more quickly (so reduce the time between Monday when the materials are purchased and Thursday when they are sold)
 - b. Or buy fewer materials, make your products with that, sell them and go back to make more before your other expenses are due (so on Monday & Tuesday)
4. Purchase fewer materials. If your fixed expenses for the week are R460, then you only have R40 to use on materials
5. Try to negotiate with you supplier to pay them at the end of the week (on the 2nd Friday)
6. Employ someone to sell for you so that as you make a chair, they go out and sell that chair so you get income coming in each day, instead of only on Thursday

7. Alternatively, perhaps your landlord will allow you to pay rent later or you could negotiate with your staff to pay them later

Group Exercise 1:

You are planning your cash flow for the final week of the month. If you can sell 9 products at R100 each, how many items must you sell each day so that you are able to meet your various expenses?

Day	Details	Amount	Cash Flow Analysis
Friday	Cash on Hand	500	500
Monday	Purchase wood for chairs	200	300
	Purchase paint, nails & glue	75	225
Tuesday	Allowance for unplanned expenses	60	165
Wednesday	Salaries & Wages	250	-85
Thursday	Payment of rent	150	-235
	Sale of products	900	665
Friday	Profit for the week	665	665

Some income is required on Tuesday and Wednesday to enable you to get through the negative cash position that will occur on Wednesday.

Day	Details	Amount	Cash Flow Analysis
Friday	Cash on Hand	500	500
Monday	Purchase wood for chairs	200	300
	Purchase paint, nails & glue	75	225
Tuesday	Allowance for unplanned expenses	60	165
Tuesday	Sell 2 @ R100		200
Tuesday	Net cash on hand		365
Wednesday	Salaries & Wages	250	115
Wednesday	Sell 1 @ R100		100
Wednesday	Net cash on hand		215
Thursday	Payment of rent	150	65
Thursday	Sale of remaining 6 @ 100		600
	<i>Total Sales for the week</i>	<i>900</i>	<i>900</i>
Friday	Profit for the week	665	665

Selling at least 2 chairs on Tuesday prevents you going bankrupt here.

Selling at least 1 chair on Wednesday prevents bankruptcy here.

This example shows that you have to sell at least 2 chairs on Tuesday and at least another 1 more on Wednesday to have sufficient cash to cover the timing of the week's expenses. To be safe, it may be wise to target to sell 3 on Tuesday, 3 on Wednesday and 3 on Thursday.