

Oh No! I'm Out of Cash Again!!

By David Lewis

Many owners of profitable small businesses cannot understand how they get in a cash crunch dilemma on a regular basis. Their accountant assures them that they are really making money and they pay taxes on the profits, but the balance in their bank account is often in the red. This predicament is generally caused by inadequate management of two huge cash consumers most small business owners cannot avoid: inventory and receivables.

Managing inventory levels and types is challenging to most small business owners. Not only is it hard to try to anticipate customer tastes and the demand for certain products, but vendors often engage in quantity discounting practices that encourage over buying to “save money.” On top of that, it is much more fun to buy if you can get products now and not have to pay until later. In addition to buying too much, most

owners also discount their old inventory too slowly. Learning to view inventory as precious cash that is actually shrinking in value every day is a very valuable skill.

Properly managed receivables can be an effective tool for acquiring additional sales and market share, but if not properly managed, the accounts receivable drains the cash out of a business—especially one that is experiencing rapid growth. A potential new customer's repayment ability and practices should be checked with both banks and other vendors prior to issuing credit. Calling early and often is very effective when trying to keep your customers on target with their payments on account. An effective strategy to reduce the level of your receivables is to offer cash discounts for early payment, such as the widely used 2%, net 10 example.

Effective inventory management starts with developing accurate sales projections based on past performance and estimating the effectiveness of your marketing plan. Keeping receivables consistently current involves a standard credit checking policy and an assertive and proactive collection effort. Both cash crunch issues are manageable even if they cannot be avoided completely, and with planning, foresight, and a little luck, small business owners can avoid getting into cash crunch situations.

The first step to effective management is proper planning. Business owners should regularly use their business records and financial statements to look for sales and expense trends and compare current information to both historical data and industry averages to develop business strategies. Finally, a budget supporting these strategies will

outline the financial implications of decisions like purchasing levels, credit limits, and borrowing needs. If you predict cash shortfalls before



they occur, you can arrange for other financing to get you over the rough spots with little negative impact on your business and avoid the “Oh No! I'm Out of Cash Again!” situation.

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