Harnessing the power of your cash flow

Four Essential Tips for Small Business Growth

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Introduction

From chasing down late customer payments to trying to perfectly time your expenses—all while operating your business—managing your cash flow can be a struggle. Some days you're on top of the world with plenty of cash to cover all your operating costs. Other days you're crossing your fingers hoping a recent invoice gets paid on time so you can make payroll.

If that sounds familiar, you're not alone. According to a study from Intuit, 61% of small businesses struggle with cash flow. What's worse is the impact of cash flow problems go beyond occasionally making you late for a payment. If mismanaged, it can cause you to:

- Not pay vendors
- Default on loans
- Operate at a loss
- Go out of business

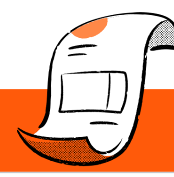
The good thing is that with some tweaks, you can not only avoid these problems, but also optimize your cash flow to a point where it's no longer keeping you up at night. In this guide, we'll cover four cash flow optimization tips that can transform your company's financial future.

Understanding your cash flow

Cash flow is the amount of money that comes in and out of your business.
Whenever cash enters the business (product sales, selling assets, etc.) or exits the business (paying salaries, monthly utilities, etc.) it positively or negatively affects your cash flow.

Positive cash flow = You have more cash coming in than going out
Negative cash flow = You have more cash going out than coming in

This movement of cash is recorded in your cash flow statement, which is one of three major financial statements for businesses.



Financial statement	What it tells you
Cash flow statement	Where money comes from (cash inflows) and where it goes (cash outflows).
Balance sheet	All of your company's assets, liabilities, and shareholder equity.
Income statement (P&L)	How much money was earned (income) and how much was spent (expenses) during a given financial period.

The income statement and balance sheet show segments of cash activity. However, the cash flow statement bridges the information from these two statements to show the complete picture of your company's finances.

Bridging the gap with cash flow

Example

A new business shows a $10,000 loss on its income statement in one month. But in that month, the business also secured a $100,000 investment (which shows up on the balance sheet), which means the business is cash flow positive (which shows up on the cash flow statement).

Similarly, a business that records a $1,000 profit but makes a $5,000 payment towards a loan (on the balance sheet) is cash flow negative (on the cash flow statement).

By combining the information from all three financial statements, you get the full picture of how cash moves through the business.

How a cash flow statement is organized

Profit and Loss | Balance Sheet | Cash Flow

Options: Legend:

Cash Flow Breakdown (Collapse All)	Jul '22 Actual	Aug '22 Actual	Sep '22 Actual	Oct '22 Actual	Nov '22 Forecast	Dec '22 Forecast	Jan '23 Forecast
Operating Activities	**-$152,473**	**-$147,615**	**-$142,190**	**-$137,061**	**-$132,158**	**-$126,731**	**-$121,576**
Operating Activities (excl. Worki ...	-$152,740	-$147,619	-$142,492	-$137,359	-$132,219	-$127,702	-$121,918
Net Income	-$152,000	-$149,000	-$144,000	-$139,000	-$134,000	-$129,000	-$124,000
Depreciation and amortization	$1,260	$1,381	$1,5080	$1,641	$1,781	$1,928	$2,082
Changes in Working Capital	$267	$4	$302	$298	$61	$341	$342
Prepaid expenses	$568	-$535	$601	$526	-$492	$557	$482
Accounts receivable	$125	-$138	$152	$167	$184	$202	$222
Other current assets	-$426	-$401	-$451	-$395	$369	-$418	-$362
Investing Activities	**-$30,673**	**$5,900**	**-$6,136**	**-$6,381**	**-$6,636**	**$5,323**	**-$7,177**
Purchase of PPE	-£5,673	$5,900	-$6,136	$6,381	-$6,636	-$6,901	-$7,177
Purchase of property and equipment	-£5,673	$5,900	-$6,136	$6,381	-$6,636	-$6,901	-$7,177
Strategic Investments	-$25,000	$0	$0	$0	$0	$1,578	$0
Purchase of minority interest	-$25,000	$0	$0	$0	$0	$0	$0
Gain (loss) on sale of non-core assets	$0	$0	$0	$0	$0	$1,578	$0
Financing Activities	**$3,000,000**	**-$218,269**	**-$182,562**	**-$151,048**	**-$123,302**	**-$101,212**	**-$78,853**
Issuances	$3,000,000	$0	$0	$0	$0	$0	$0
Issuance of debt	$1,000,000	$0	$0	$0	$0	$0	$0
Issuance of equity	$2,000,000	$0	$0	$0	$0	$0	$0

CASH FROM OPERATING ACTIVITIES:

Cash that flows through the business as part of its day-to-day operations. This includes cash earned from sales or spent on expenses.

Examples: Sales revenue, rent, salaries, utilities, interest expenses

CASH FROM INVESTING ACTIVITIES:

When the business purchases or sells long-term assets that change in value.

Examples: Purchase or sale of property, plant and equipment (PP&E), sale of stocks or other securities, purchase of patents or trademarks

CASH FROM FINANCING ACTIVITIES:

Any debt the business tends to or acquires.

Examples: Loans, lines of credit, mortgages, equipment financing

OPTIMIZATION TIP 1

Analyze your cash flow

Understanding more clearly how much cash is flowing through your business is step one. Step two is learning how to properly analyze the data.

Cash flow analysis will give you a way to assess the sources and uses of cash in your business, and determine if you have enough money coming in to cover short-term obligations like paying your employees, replenishing your inventory, and any other uses of cash you may have.

Investigate positive cash flows

While positive cash flow is a good indicator of a healthy business on the surface, you should investigate further to understand what the main sources of cash are for a better picture of the business's financial health.

Positive cash flow scenarios

BUSINESS X

SCENARIO

Business X was cash flow positive last quarter. However, a deeper look at their cash flow statement shows that they are continually selling off assets to support business operations.

ANALYSIS

Although being cash flow positive sounds good, this approach likely isn’t sustainable long term. They will eventually run out of assets to sell.

BUSINESS Y

SCENARIO

Business Y is cash flow positive due to extended payment terms with suppliers, but they struggle to collect payments from their customers on time, leading to a significant accounts receivable backlog.

ANALYSIS

Their cash flow situation may seem positive in the short term, but their inability to manage accounts receivable efficiently could lead to cash flow constraints, hampering day-to-day operations and affecting their ability to invest in growth opportunities.

BUSINESS Z

SCENARIO

Business Z shows positive cash flow on paper, but a significant portion of their income comes from one-time, unsustainable sources, such as a large legal settlement or a one-off government grant.

ANALYSIS

Despite the appearance of positive cash flow, Business Z's reliance on non-recurring income sources creates uncertainty for future financial stability, and they may struggle to maintain profitability once these one-time gains diminish.

Dive deeper into negative cash flows

Similarly, a period with negative cash flow isn't always a warning flag, as your business could have recently made a number of large investments in property or equipment that depleted the cash balance momentarily, but will support future growth.

Negative cash flow scenarios

BUSINESS A

SCENARIO

Business A is a startup that is heavily investing in research, development, and marketing to establish a strong market presence. As a result, they have been cash flow negative for two quarters.

ANALYSIS

Being cash flow negative at the early stages is common for startups focusing on expansion and innovation. As long as their investments lead to anticipated growth and market share, it can be considered a strategic move rather than a negative sign.

BUSINESS B

SCENARIO

Business B is restructuring to improve efficiency and competitiveness. The upfront costs of the restructuring have caused a temporary cash flow deficit.

ANALYSIS

Short-term cash flow challenges during a restructuring process are not uncommon. If the restructuring leads to a leaner and more profitable organization, it can be a positive step for the business in the long run.

BUSINESS C

SCENARIO

Business C is a seasonal business that experiences higher expenses during the off-season while preparing for peak demand.

ANALYSIS

Seasonal businesses often face cash flow fluctuations. As long as they have a well-managed cash reserve to cover off-season expenses and anticipate healthy revenues during peak times, being cash flow negative temporarily is reasonable and manageable.

Calculate free cash flow (FCF)

Another way to analyze the cash flow of a business is with a free cash flow calculation. The FCF value can be a good measure of profitability because it shows how much cash your business has left after paying for operating and capital expenses.

FCF = net cash from operating activities – capital expenditures

This leftover cash can then be spent on other things to grow and add value to the business. So in general, the more FCF that a business generates, the better.

However, companies that are just getting started may not generate a significant amount of FCF until they're more established, and the number may even be negative. But, this may not be a sign of a faltering business until it becomes persistent over the long term.

Assess your debt coverage service ratio (DCSR)

Calculating your DCSR is a good way to tell if a business that is generally profitable could become illiquid and unable to cover short-term liabilities. It will show you how much cash is tied up in outstanding accounts receivables, unsold inventory, etc

DCSR = net operating income / short-term liabilities

Short-term liabilities = financial obligations that must be paid within the next year

Example:
Company X has a net operating income of $3.5 million, and short term debt of $1.5 million. Company X's DSCR is 2.33. (3.5M/1.5M).

DCSR benchmarks

Here are some helpful benchmarks to determine if your DCSR is "good" or needs improvement.

DCSR	Quality
>2.0	Great
>1.25	Good
>1.0	Not so good

Source: Investopedia

Note: The age, industry, and model of your business all play a role in what's considered a good DSCR.

Recommendation: Use Finmark From BILL to create your cash flow statement and perform this analysis all in one place!

OPTIMIZATION TIP 2

Get a handle on your accounts receivable and payable

Once you've analyzed the cash flowing through your business, the next step is to implement best practices to optimize your accounts receivable and payable.

Effective accounts receivable management ensures timely customer payments, enabling your business to meet its financial obligations and invest in growth initiatives. Similarly, best practices for accounts payable facilitate timely supplier payments, fostering positive relationships and often leading to more favorable credit terms.

Use best invoicing practices

A straightforward way to optimize accounts receivable is by prioritizing clear communication and accuracy in your invoicing.

- Ensure your invoices are accurate, detailed, and easy to understand
- Include specific payment terms and itemized charges
- Clearly define any late payment penalties or early payment discounts

Be sure to send invoices promptly and offer various payment options like virtual card, credit card, and ACH. Customers who receive your invoices quickly and have convenient ways to pay will likely pay faster.

Negotiate favorable credit terms with suppliers

Favorable credit terms with suppliers are a helpful way to optimize accounts payable and improve cash flow. Here are a few strategies you can use to help get the best terms for your business:

Relationship building:
Foster open communication and showcase your reliability through timely payments.

Volume commitments:
Offer to purchase a specified volume consistently over time.

Negotiate payment periods:
Adjust payment periods from net-30 to net-45 or net-60.

Prepayments:
Propose partial prepayments to alleviate potential supplier concerns.

Flexibility:
Approach your negotiations with a willingness to compromise for mutually beneficial solutions.

Bulk purchases:
Commit to larger order quantities to increase your bargaining power.

Early payment incentives:
Ask about discounts for making payments ahead of schedule.

Financial stability:
Present your business's stable financial position to suppliers.

Consolidation:
Combine orders with a single supplier for cost savings.

Automate billing and payment processes

Because managing accounts receivable and payable can be challenging and time-consuming, automating those processes can be a game-changer.

With automation, you can easily create and schedule custom invoices and enhance customer satisfaction by offering convenient payment options and reminders. You also gain the ability to automate supplier payments. Overall, you'll spend less time on administrative tasks and have more time to focus on growth.

Recommendation:
Use **BILL Accounts Payable** and BILL Accounts Receivable to automate and optimize your payables and receivables.

Get started
https://www.bill.com/

Read more
https://www.bill.com/case-study/customer-case-study-clif-family/

> "Overall, I would estimate that BILL has increased efficiency in our office by 20%, and personally saved me a significant amount of time."
>
> Linzi Gay, President, Clif Family

OPTIMIZATION TIP 3

Expense control and cost management

By controlling spend and expense more strategically, you can better direct funds toward initiatives that contribute to growth and profitability. Additionally, when budgets are set, tracked, and adhered to, employees become more conscious of their spending habits, and transparency and accountability improve throughout your organization.

Identify areas of unnecessary expenses and waste

Thoroughly analyze spending patterns, categorize expenses, and compare them over time to spot irregularities. By breaking down expenditures into categories like office supplies, travel, and software subscriptions, businesses can pinpoint areas susceptible to overspending.

Regularly comparing budgeted expenses to actual spend can help identify overruns. Additionally, benchmarking spend against industry standards or similar businesses can clearly show where adjustments are needed. It can also be helpful to talk to employees as their insights can provide a front-line perspective about areas of improvement.

Techniques for reducing overhead costs

Reducing overhead costs can be tricky, but a few useful techniques can help.

Have regular vendor negotiations: Make it a point to have regular conversations with suppliers to secure better terms, discounts, or bulk pricing.

Prioritize expenses: By ranking expenses based on their direct impact on core operations, you can make more informed decisions about areas when you can cut spend.

Use detailed budget planning: Creating a specific plan enables departments to more easily adhere to spending limits.

Explore energy-efficient practices: By reducing utility expenses over time, you can cut related costs.

Automate expense management

Automation can also be transformational for spend and expense management. For example, BILL Spend & Expense combines free software with corporate cards to provide a seamless experience for requesting, spending, and tracking your business finances.

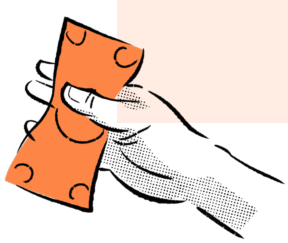
You can reduce manual data entry, speed up reimbursements, avoid human error, and set spend controls to ensure you always stay within budget.

Recommendation:
Use BILL Spend & Expense to get more visibility and control over budgets and expenses.

Get started
https://www.bill.com/product/spend-and-expense

Read more
https://www.bill.com/case-study/customer-success-story-polystone-planters

> "BILL Spend & Expense saved us 75% of the time on entering the advertising expenses because I don't have to do data entry."
>
> Karen McCubbin, Accountant, PolyStone Planters



OPTIMIZATION TIP 4

Test your assumptions

Some cash flow problems can be prevented in advance with proper planning. One of the best ways to do this is to model your assumptions before you take action. This goes for any changes that may significantly impact cash flow.

Thinking of increasing your prices? Model it.
Planning to hire a new group of employees? Model it.
Launching a new marketing campaign to acquire more customers? Model it

Modeling your plans and scenarios

Modeling your plans beforehand allows you to forecast the impact these changes may have on cash flow. However, the key to modeling your assumptions is to test various scenarios. We recommend modeling at least three scenarios for any significant changes:

Scenario	Assumption	Plan of action
Baseline	Conservative impact on cash flow	Make little to no changes to the plan in the short term.
Upside	Positive impact on cash flow	Consider how to capitalize on the positive impact made by your changes.
Downside	Negative impact on cash flow	Pull back on the changes made or consider pivoting to offset any losses.

This process of creating and comparing multiple scenarios is called scenario analysis. In addition to allowing you to plan for the good, bad, and the ugly, scenario analysis also makes it easier to gauge whether or not your plans are financially feasible.

Modeling example: Bob’s Window Cleaning

Let’s look at an example of how a business can use scenario analysis to gauge the potential impact of a price increase on cash flow.

Bob’s Window Cleaning is planning to increase their prices by 20% for new and existing customers. But before they make the increase, they want to make sure they’re prepared for any positive or negative impact this may have on our cash flow.

Scenario	Assumption	Plan of action
Baseline	The balance of lost customers due to the price increase is offset by the additional revenue from new customers. Cash flow will remain consistent in the short term but cash inflows will grow long term.	Stick to the plan and monitor the long-term impact of the higher prices. Regularly compare actual performance to projections.
Upside	Very few customers cancel, and the current customer growth rate stays consistent. Due to the increased prices, cash flow improves significantly.	Consider re-investing the additional revenue into marketing, better equipment, or new team members to further speed up growth.
Downside	A significant number of customers cancel due to higher rates, and new customer growth slows down. As a result, cash inflows dip moderately.	Revert back to older pricing for existing customers and model how that will impact cash flow.

Modeling example: Bob's Window Cleaning contd...

In the modeling example, you can see how your plan of action adjusts based on each potential scenario. This fictional business can create thresholds for when each plan of action should be initiated. For example, if X% of current customers cancel their contracts and new customer growth slows by Y%, the downside scenario may be put into action.

On the other hand, if customer churn is less than X%, and new customer growth remains at least Y%, they can follow the upside plan. Setting these types of thresholds makes it easier to prepare and plan your next steps.

Recommendation:
Use Finmark From BILL to quickly create and compare multiple scenarios and test your assumptions!

Ready to harness the power of cash flow?

Discover how Finmark from Bill can make managing, forecasting, and analyzing your cash flow easier. Get started with a free trial today!

Profit & Loss | Balance Sheet | **Cash Flow Statement**

Options: | Legend:

Cash Flow Statement	May '23 Actual	Jun '23 Actual
Operating Activities	$83,137	$90,392
Net Earnings	$81,766	$88,691
Changes in working capital	$325	$655
Depreciation and amortization	$1,046	$1,046
Investing Activities	$3,000	$3,000
PP&E	$3,000	$3,000
Financing Activities	-$2,500	-$2,500
Debt Repayment	-$2,500	-$2,500
Net change in cash	$83,637	$90,892
Cash, Beginning Of Period	$293,457	$375,223
Cash, End Of Period	$375,223	$463,914

Get started