

The Credit Crunch and the importance of Cash Flow

Companies and individuals who do not pay their bills in a reasonable time stump your growth and cause the inability for you to settle your accounts on time. This can affect your ability to negotiate better pricing and will reflect on your goodwill. This is not your fault but you can do something about it.

I have seen good businesses go broke because of bad debts. A snowball that is the thorn in the side if New Zealand business all for a few simple steps that will deter bad debts.

Cash flow is the number one problem facing small and medium enterprises.

If everyone paid their account on time the economy would be far better off including cheaper products. This will not happen but you can improve your chances and get paid sooner. The moment that a business grants credit it will lose 3% of its money, not a lot, but when an owner profit is base on a 10% profit margin this does impact on competitive pricing and the owners income not to mention service his debt.

An account that is 30 days overdue means the loss will increase radically to where the business can expect to lose 5%. Still not a lot but at an account that is 90 days overdue the sale will lose 20% of its initial value. At this stage the profit is now gone and it is now a case of recuperating some costs, the business would have been better off not trading. The more days and months waiting for payment the more likely a business will not be paid. The average payment in New Zealand is 45 days and will reach 55 days in some months.

When a supplier prices his stock or quotes for a project they do not often allow for the payment to late, but no one pays on the 20th of the month right?

Large companies have the luxury of in-house professionals such as credit managers who monitor the debtors and place accounts on stop credit without the fear of drop in supply as a company. They even have credit policies that state when to phone customers and make arrangements and even place limits on accounts. In a small business and medium business, the owner or accounts person must try to please everyone and may fall into the trap of "supply or I will lose the customer". The major problem is time and skill. Their are outsource credit managers available to help just as large companies have in house accountants but most businesses use an outside accountant.

How do you start, solve or prevent the issue?

The first step is to know who you are dealing with and get a firm agreement of the terms and conditions of the sale. One is to draft a Credit Application and a Terms of Trade.

A credit application has several purposes. One is a clear authority to check your customer credit worthiness; under the privacy act you cannot do this without the customer's approval that the credit application will give. The second purpose is that you get to know your customer from who your competition is. I had an instance the other day where I ran a check for a paint company for a trade customer and found that he had 3 accounts with the competition. Why was he shifting? Stop credit problems? It turned out that he was unhappy with the service and pricing and so the new supplier could allow for this in his pricing and keep the customer permanently.

A common thought that a non perfect credit rating or incomplete information means a "NO" is inaccurate and turning a potential good customer away does not make good business sense. There are ways to still protect yourself, among these may be limiting credit or a probation period of good trading to keeping the account strictly to terms this may extend into a personal guarantee of the limited companies owner.

Terms of Trade is an agreement that is agreed and must be signed by the customer before any transaction takes place. Telling the customer of any condition such as overdue interest or even the date the account is due on the invoice is too late. On the wall is also not sufficient as the customer has not agreed to it. As with all agreements both parties must agree. If any problem eventuated the supplier must have to show that the customer agreed to the terms before the transaction takes place. Having it on the invoice does not give the customer the opportunity to agree to these conditions. Interest and collection costs cannot be claimed unless it is agreed in the terms of trade or by the court. Court action sounds expensive, and it is.

If things go wrong, the company has far better protection and will save money with a correct credit application and terms of trade. It is quit acceptable to ask for this to be signed. They are common but it is surprising the amount of company's that do not get them signed. Put it this way, go to the new bank and get \$100 overdraft and see how many forms are required. Suppliers are giving away hundreds and thousands of dollars of stock and services (or cash, same thing) sometimes they are not sure if the customer is a company or not or even there last name, laugh, it happens regularly. In these cases more

often when you supply John down the road who is a mate of a mate you will not be paid without expense if at all.

Many clients have said to me time and time again, that they feel uncomfortable asking a potential customer to sign a Credit Application and Terms of Trade. I often hear "I've dealt with him for years... he's fine" or "he's a friend" these people then often get a good price and take advantage of this. This turns into an extended credit terms then I often hear "good guy but he keeps on giving me excuses" or "I haven't spoken to him for ages but he's fine". This puts a dampener on any relationship, better to be professional with business from the start and make a firm agreement if everything goes as it should, a great relationship can still flourish without anyone being ripped off.

Everyone expects to hand over information about themselves or their company when they are getting credit without these small and medium business leave themselves vulnerable to loss. A major reason for company liquidations are cash flow issues.

When I first started in credit management some 20 years ago my boss said to me "it's your family or theirs" true but I have learnt with my own experience that you can "help people get what they want so you get what you want".

Finally prevention is much cheaper than the cure.

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Link Receivables

Link Receivables Ltd is a complete professional outsource credit management solution for businesses and promotes non-aggressive credit control using specialised, efficient and proactive methods.

They offer a full range of accounts receivable and credit control solutions for business from consultancy to collection and every step in between. If you would like contact Link Receivables, please contact Dean on (03) 339 6438 or email info@linkreceivables.co.nz. Alternatively you can visit www.linkreceivables.co.nz.