2020 foresight: six steps to avoid your next *Dash4Cash*

It doesn't take a crystal ball to know what your company is going to be doing in the weeks running up to June: if your business is like a lot of others, the end of the fiscal year will be accompanied by a flurry of activity I call the *Dash4Cash*.

If you stop replenishing stocks for a week or two, delay payments to suppliers beyond terms, and chase your customers who are used to your otherwise lax collection activities, your cash flow statement will look a lot better – briefly. But a few weeks after all that effort, you are almost certain to be back where you were before the Dash, and maybe even a little worse off because your team wasted most of June trying to make your financials look better artificially.

I am not sure why so many businesses repeat this push year-on-year. Anything beyond a superficial look at a company's financials will expose the annual cycle. It negatively impacts customer and supplier relationships and will eventually influence long-term profitability. So, it's not fooling anybody outside the company and it's likely not fooling anybody inside the company either.

Fortunately, there is a superior alternative to pretending to be in shape. It's called being in shape. Not many companies do it, but if you do, your business is likely to enjoy a number of advantages, including increased free cash flow, lower balance sheet risk, and a lower cost of capital once lenders see your new and improved financials. Typically, this even comes with efficiency gains, particularly if you employ new technologies like Robotics Process Automation ('Digital Workforce') to drive down the cost of your back-office processes.

Getting there is not as hard as you might think, particularly if you start now. Here are six tips every business should consider ensuring the Dash4Cash can be avoided – once and for all!

1. Understand what goes wrong

For individuals, behavioural scientists say one of the most important steps toward breaking a bad habit is to understand why you do it. When it comes to lax working capital management, most of the problem is driven not by weakness but an urge to succeed – a sales team offers longer payment terms to close a deal, for instance, or the logistics team keeps extra inventory on hand just in case a customer might request it (but historically never did). Once you know the reasons for the behaviour, you can begin to give the organisation an even better set of reasons to follow working capital best practices. For example, eliminating slow moving and obsolete stocks ('Slobs'), use statistical methods to manage moving stocks, improving collections performance sustainably and negotiating longer supplier terms will give you a permanent cash release available for investments in capital expenditure, acquisitions or to fund debt reduction.

2. Get paid

Chances are good that your company operates on the Pareto principal, in that 20% of your clients are responsible for 80% of your business. If that is true for you, you should focus most of your energy on making sure you have clear contractually agreed payment terms that are as favourable as possible (and adhered to) with the relatively small number of clients who make up the bulk of your business. Understand the payment behaviours of each customer and define strategies to deal with them, for example, are they a 'big, notoriously bad payer' vs. a 'small good payer who missed one payment'. And hold your customers accountable should they deviate from the agreed terms. Credit and collections policies are too often disregarded in order to preserve 'the client relationship' at the expense of the companies' cash flow. Adopt a very clear process for following up missed payments – a staggered combination of phone, text, letters and in person meetings should be utilised to ensure customers understand you are not a 'bank' and expect to be paid on time.

3. Do the maths

Customers are always looking for excuses to avoid payment, but you don't have to give them any. Automate your invoicing system and keep your errors to a minimum. Have bots send automatic reminder letters, create statements and daily reporting to provide customers with a clear picture of the current position and payment profile for their account. Make 'grace periods' a day of the past.

4. Clock your inventory

Once you understand which of your products are slow moving, you know where you can safely trim your stock. Also understand the regularity of demand and manage your stocks and safety buffers accordingly – have the right stock at the right time, and not too much of most products. Understand that stock management is science, not art, stocks have to be optimised one-by-one, with statistical methods and efficient tools and not 'experience'. Do not believe your existing system does it all for you, in many cases even the smartest systems are knocked out by humans inputting suboptimal parameters due to a lack of understanding of best practice inventory management.

5. Raise your transactional reporting game

Too often, sales teams extend easier payment terms without understanding the full impact of this action on business. Front-line managers need to be able to see the impact of working capital decisions on the broader business, transparency and the right incentives are key. Use analytical tools to understand individual customer margins and the cost of capital associated to the payment terms – don't give good terms to bad customers.

6. Measure it!

People usually won't do what you don't ask them to do. Setting working capital metrics as part of your managers' KPIs will keep them more focused on achieving lean working capital accounts.

Most incentive systems these days include cash metrics such as DSO (Days Sales Outstanding, Debtor Days), or EBITDA to cash conversion, which impact eligibility for bonus payments or promotion. Without these it is very easy to prioritise revenue and profits over cash flow performance. We've all learned that revenue is vanity, profit is sanity, but cash flow is king. Does your incentive system encourage positive business behaviour?

As psychologists will tell you, overcoming bad habits is a matter of staying focused on the advantages of a new set of behaviors. In this case, you should try to keep your team focused on the many positive and sustainable advantages of smarter working capital management rather than the few short-term advantages of a lax approach to working capital.

If you want to avoid that awful June dash, you have to start soon. Awareness is the first step to overcome bad habits – educate your team and yourself. A typical chartered accountant has a general understanding of working capital, however, at FTI Consulting we have dedicated working capital specialists who know the best practices that can deliver 20% - 40% improvement in cash opportunity, sustainably, now. Give us a call today to discuss how we can help you eliminate the painful Dash4Cash each year.

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