How to Shorten a Cash Flow Cycle

Methods and practical ways to shorten prolonged cash flow issues.

Diagram

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In a turbulent and unreliable economy, cash can make or break your business much quicker than you may anticipate. Between waiting for invoices to be paid or not having enough cash to purchase inventory, whatever the issue, there is likely a reasonable solution out there… it’s just a matter of knowing what that solution is!

So, you may be wondering how your business can shorten a cash flow cycle to avoid some of these problems.

Stay tuned for some strategies to create a quick cash flow cycle for your business, including:

* Outstanding Receivables
* Client credit check procedures
* Reduced terms
* Better follow-up
* Practical assignment of terms
* Factoring

**Outstanding Receivables**



Collecting outstanding receivables is one of the quickest ways you can significantly impact your cash flow cycle. This is money that is already owed to your company, so collecting on receivables that are due will instantly boost your cash flow and in addition, will settle some of your customers’ outstanding accounts.

You can also improve your cycle on future receivables by offering a small discount for upfront or early payments, or even require upfront payment/deposits for certain products or services. Some businesses require upfront payment on new accounts. Only when they trust their partners do they extend the terms.

If you’re looking for a shorter cash flow cycle, you can aim to keep credit terms at 30 or fewer days and have your accounting department (maybe that’s you, too?!) follow up or send regular/automated reminders to ensure on-time or early payments.

Continue to regularly follow up with past-due receivables because every passing day means they are less likely to be paid. Sometimes, if the relationship is not salvageable, it is worth it to use a small claims collection agency and the commission is worth it to have some of the receivables paid.

**Client credit check procedures**



If a customer is new, offering them shorter credit terms and requiring a credit check (even for orders that may be on the smaller side) can be a good idea to avoid getting tied up in accounts receivable or collection agencies in the future.

Establish policies for when a client credit check would be required and when your sales team can override this credit check (if at all).

If a new customer wants to make large purchases on a regular basis, it might be a good idea to establish some terms like a required background and credit check.

**Reduced terms**



Depending on your industry, it is very possible that you could reduce your terms overall in order to shorten the cash flow cycle. Customers who object to this are likely not customers you want to have in your cash flow cycle, but you can ease them into this new process by sending out communications regarding the upcoming changes. So maybe sending them a message saying their next cycle will be on reduced terms as the business transitions will give them enough leeway.

People understand that the business climate is changing in the current economy, so these changes shouldn’t be unexpected.

Reducing your terms can also help you to weed out bad customers - if they can’t hit your reduced terms on a small order it’s better not to be in the hole on this one.

**Better follow-up**

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How you follow up with customers often dictates how quickly cash flows into your business via bills that are paid.

Honestly, sometimes the only reason bills aren’t paid on time is because the client didn’t receive a friendly reminder. And while it’s not your responsibility to remind your clients to pay their bills, it is your money that you are owed, so keeping track of it should be one of your top priorities.

By following up regularly with your clients you can also improve your relationship and rapport with them which could also lead to increased sales or you becoming a preferred vendor/being referred to their associates.

**Practical assignment of terms**

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Considering a practical assignment of terms for your customers is important because as we mentioned, if a client is looking to purchase large sums on a regular basis, it might make more sense to provide longer payment terms provided they pass the background and credit check. On the other hand, you could require them complete a few shorter-term payments or pay their bills on time before extending the terms for them.

If a client is looking for a short amount on a one-off or less frequent basis, it might make sense to have shorter terms with higher interest, in addition to a quick credit check. Anyone who objects to this process creates a potential red flag as someone you don’t want to do business with. They will likely make you chase them or do not ever intend to pay on time in the first place, which is something you do not want to deal with.

**Factoring**



Factoring is the action of “selling” or financing an accounts receivable invoice before your customers actually pay the invoice.

For example, if your customer is on a net90 schedule but you need cash sooner than that (and you know they’re good for the invoice), you can factor or “sell” the invoice and pay back your financer when the customer pays on time.

This is a risk if the customer does not pay on time or does not pay before your financing is due, so factoring your accounts receivable (while a great way to make fast cash before your AR is actually due) can be a risk.

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If cash flow has been an issue lately, try starting with collecting outstanding receivables and slowly implementing more of these strategies from that point onwards.

You want collecting accounts receivable and improving your cash flow to be a natural process that integrates well with your current method of accounting and doing business, so don’t do anything that’s unnatural to you, or get the advice of your accountant before proceeding. They can help you to forecast the potential impact of a strategy on your cash flow cycle.

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If you feel you could benefit from a practical and experienced fractional CFO, please connect on LinkedIn and message me to set up a time to discuss what you would like to accomplish within your business and a plan to get you there.

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