SHORT TERM CASH FLOW MANAGEMENT
High level guidance notes

In the current crisis, management of cash is critical to ensuring business survival until a return to more normal conditions occurs. BDO has prepared this brief guide to cash management specifically for young technology and science-based companies, including university spin-outs.

To manage cash and minimise cash outflow, companies should:

- Prepare a base case receipts and payments short term cash flow forecast to identify the cash needs of the business
- Use the forecast as a tool to identify opportunities to minimise cash flowing out of the business, overlaying these on the base case forecast.

SHORT TERM CASH FLOW FORECASTING

- A short term cash flow forecast models receipts and payments on a weekly basis for the next 13 weeks
- They are built up line by line to provide maximum visibility and flexibility
- For every receipt or payment that is input, the aim should be to support the quantum and timing with presentable evidence or a robust assumption.

What is a short term cash flow forecast?

- Receipts & payments based – actual in and out cash flows
- Weekly forecast – covering 13 weeks and updated weekly
- Cash focused – start point is the opening bank position
- Simple and robust (eg Excel based) – not over-engineered
- Bottom up – uses base level data
- Management review is essential for a successful process
- Needs input of operational management
- Must be possible to extract actual data to compare to forecast weekly for variance analysis
- Takes 3-4 hours to complete per week per person
- An iterative process – accuracy will improve over time.

What are the building blocks of a short term cash forecast?

Three key principles:

- What you know **has** already happened - events that have already happened where you know the opening position or the balance that will unwind over the forecast period e.g. the opening cash/bank balance or the unwind of existing trade creditors
- .What you know **will** happen - payments that you know are going to happen over the forecast period, for example underlying regular payments such as wages and salaries, rent, occupancy costs or Interest payments or receipts
- What you think **might** happen - transactions which have yet to happen that will convert into cash over the forecast period, for example forecast payments arising from transactions that have yet to occur eg purchases yet to be made, asset sales or fixed asset purchases.

What goes wrong?

- Overstating sales forecasts (probably not an issue for early stage businesses)
- Understating costs
- Ignoring historic trends or performance of customers and suppliers
- Understating cash inflows/outflow delays
- Making “overly optimistic” assumptions
- Seeking increased forecast accuracy whilst overlooking the required process oriented improvements
- Preparing top-down forecasts in isolation of detailed business unit input
- Lack of ownership and accountability for the forecast.

KEY ISSUES TO CONSIDER

- Speed v simplicity
- Who reviews the forecast?
- Who gets the reporting pack and what do they do with it?
- Process for preparation – always keep the previous forecasts!
- Daily, weekly and monthly cash routines.

CASH MANAGEMENT – RECEIPTS

- Debtor receipts - pursue overdue invoices and agree payments dates with customers to provide greater certainty to your cash flow forecast
- Forecast sales - cash from sales not yet made are likely to be difficult to estimate (or non existent) for some businesses and the payment dates are even more difficult to determine. If customers have prepaid deposits, you will need to ensure your cash flow represents the balancing receipt only
- Other - If you are expecting cash from any other source, agree the timing and values through formal correspondence as receipts can often be large in quantum and have a significant impact on your cash balance.

GRANTS AND GOVERNMENT SUPPORT - guidance for support available to businesses is available at https://www.gov.uk/coronavirus. Key highlights include:

- Coronavirus Job Retention Scheme (CJRS) if you need to furlough employees
- Statutory Sick Pay relief package for businesses with (<250 employee)
- Grant of £10,000 for all business in receipt of small business or rural rate relief

The timing of cash from these schemes will vary so seek payment dates where possible.

CASH MANAGEMENT – PAYMENTS

It is critical to understanding which payments can be minimised or the timing of payment negotiated in order to minimise cash outflow:

- Wages and salaries – typically paid weekly or monthly, and ordinarily easy to estimate. In the current circumstances, the ability to pay with no/reduced cash inflow is likely to be challenging. Consider furloughing employees, reducing working hours, permanently reducing headcount, putting in place pay cuts, or experiencing higher levels of sick leave, all of which will require recalculations. It is best not to net off any grants you may receive via the CJRS as the timing of your payroll and incoming grants may be different
- PAYE - typically payable to HMRC on the 19th day following month end. Consider a time to pay arrangements with HMRC with respect to current and future liabilities
- Trade creditors - identify supplier invoices which need paying urgently and those which may require greater flexibility. Consider categorising suppliers into 3 buckets – critical (must pay), ongoing (need to pay) and ad hoc/one off (avoid paying if possible)
- Ongoing development costs - identify goods or services required in order to continue development work over the forecast period. Use any stock on hand first, whilst bearing in mind buffer levels to avoid any shortages due to any supply chain disruption issues
- Rent and rates - contact your landlord and local authority to discuss a payment holiday or the ability to pay monthly if you are paying quarterly in advance
- Direct debits - review direct debits to identify any payments which may require rearranging. You may even identify payments which are no longer required
- Other overheads - overheads that are paid on invoice such as utilities, IT, waste and so on. Contact providers to discuss extending payment terms
- Loan payments - contact your lender(s) to discuss a capital repayment holiday
- VAT - If you are a UK VAT registered business and have a VAT payment due between 20 March 2020 and 30 June 2020, you have the option to defer the payment to 31 March 2021
- Other cash outflows – defer any discretionary spend not committed eg asset purchases.

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PRACTICAL CONSIDERATIONS

- Forecasting process – it is important to start with a base case forecast before incorporating mitigating activities to manage receipts and payments – as this indicates the quantum of the steps needed to address the potential funding requirement
- Receipts – discuss with your customers/funders the possibility of early/staged payment to maintain cash coming into the business. There may be significant commercial leverage with certain customers which could be used to accelerate receipts. Early and open engagement with customers/funders is critical in this respect
- Payments – given the current circumstances outgoings are potentially negotiable, even if the cost has already been incurred. Timely and open communication with suppliers is critical in agreeing deferment plans. It may be helpful to think of the position from the supplier's point of view and use that in your negotiations. For example, how important are you as a customer to that supplier?
- Landlords – it is important to consider the commercial position of landlords when seeking to negotiate rent reduction or deferment plans. For example, what alternative use is there for the building you occupy if you vacate it? Are there other tenants who you could speak with and approach landlord together with incremental leverage?
- Cost reduction – each and every line item of spend should be critically assessed and everything that is not essential to keeping the business going should be stopped or deferred.
- Self help - consider redeploying staff to perform simple tasks which may have previously been bought in (e.g. cleaning and catering)
- Directors duties – in managing the cash position and negotiating with funders, customers and suppliers, the directors should consider the financial position of the business. Where there are concerns over the solvency of the business the directors should be aware of their duties and seek legal/professional advice
- Open and clear communication - the current environment is unprecedented and managing the cash position of the business is likely to require the support of all stakeholders. In many cases this may be essential if the business is going to survive. Open, clear and honest communication with employees, customers and suppliers will be essential to gain the support of these different stakeholders groups.

IF YOU WISH TO DISCUSS ANY OF THESE ISSUES PLEASE CONTACT:

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