The 1% Cash Flow Solution

Small Changes that Make a Big Difference

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1. Price Increase

- Company annual sales: $1M.
- Raise prices 1% across the board.
- $10,000 additional profits!

Analyze pricing for all services and products

2. Sales Volume Increase

- If sales volume increases 1%, then gross profit and net profit increase by gross profit margin **x** sales volume increase.
- Current sales: $1,000,000. Gross Profit Margin: 60%.
- Increase in Gross and Net Profit: $1,000,000 **x** 1% x .60 = $6,000

Sell more

3. Cost of Goods Sold Reduction

- If cost of goods sold are cut by 1%, then gross and net profit increase by the 1% reduction of current COGS.
- Cost of Goods Sold: $400,000.
- Increase in Gross and Net Profit: 1% x $400,000 = $4,000.

Negotiate better prices with suppliers

4. Overhead Reduction

- If overhead costs are reduced by 1%, then net profit will increase by 1% of total overhead cost.
- Overhead: $450,000.
- Increase in Net Profit: 1% x $450,000 = $4,500.

Analyze expenses monthly

Profit ≠ Cash

Profit and Loss

	January	Feb.	March
SALES	$20,000	$30,000	$45,000
COGS	$12,000	$18,000	$27,000
GROSS PROFIT	$8,000	$12,000	$18,000
EXPEN-SES	$10,000	$10,000	$10,000
NET PROFIT	**($2,000)**	**$2,000**	**$8,000**

Cash Flow

	January	Feb.	March
START CASH	**$10,000**	$0	($22,000)
CASH IN	$0	$0	$20,000
CASH OUT	($10,000)	($22,000)	($28,000)
END CASH	$0	($22,000)	**($30,000)**

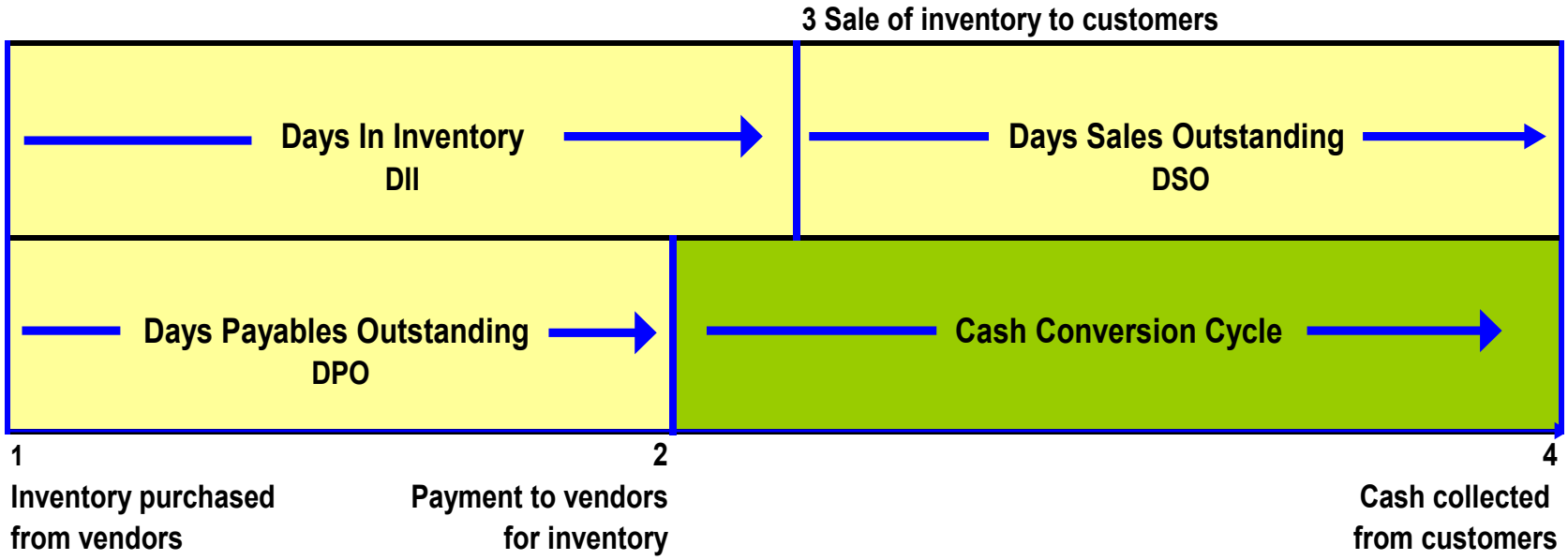
Assumptions:

Company starts with $10,000 cash.

Company pays vendors in 30 days.

Company collects from customers in 60 days.

Cash Conversion Cycle



Cash Conversion Cycle = Time from paying vendors to collecting from customers

Cash Conversion Cycle = DII + DSO - DPO

GOAL: Minimize Cash Conversion Cycle

1. Increase DPO (move line 2 to right - take longer to pay vendors)
2. Decrease DSO (move line 4 to left - collect faster from customers)
3. Decrease DII (move line 3 to left - sell inventory faster)

5. Days Sales Outstanding Decrease

Days Sales Outstanding (DSO)

DSO = 360 Days/Accounts Receivable Turnover

DSO = 360 Days/(Annual Sales/Accounts Receivable)

- DSO is the average time it takes a company to collect cash on credit sales.
- If DSO is reduced by 1 day, then cash flow would increase by 1 Day x (Annualized Sales/360).

- 1 x ($1,000,000/360) = $2,778

Average Daily Sales

Collect Faster

Tactics to Reduce DSO

- Ask customers for deposits.
- Ask customers to pay sooner. For example: Net 15 instead of Net 30.
- Provide discounts to customers who pay on time or in advance. For example: 2%; Net 15.
- Invoice faster.
- Friendly reminders before deadline that payments are due. For example: 5 days before due date.
- For recurring invoices, obtain credit card authorization from customers to automate on-time payments.
- Improve communication with customers. Understand why your customers are paying late.

6. Days In Inventory Decrease

Days In Inventory (DII)

DII = 360 Days/Inventory Turnover

DII = 360 Days/(Costs of Goods Sold/Inventory)

- DII is the average time it takes a company to turn over their inventory.
- If DII is reduced by 1 day, then cash flow would increase by 1 x (Annualized COGS/360).
- 1 x ($400,000/360) = $1,111

Average Daily Purchases

Reduce Inventory

7. Days Payable Outstanding Increase

Days Payable Outstanding (DPO)

DPO = 360 Days/Accounts Payable Turnover

DPO = 360 Days/(Costs of Goods Sold/Accounts Payable)

- DPO is the average time a company takes to pay trade invoices.
- If DPO is increased by 1 day, then cash flow would increase by 1 x (Annualized COGS/360).
- 1 x ($400,000/360) = $1,111

Average Daily Payments

Take full advantage of payment terms

1% and 1 Day Solution Worksheet

Seven Levers to Improve Cash Flow: The 1%/One Day Solution

Enter data in green cells

LEVER	LEVER DESCRIPTION	SOLUTION		APPLICATION	ANNUAL IMPACT ON CASH FLOW
1	Price Increase %	1%	x	Annualized Sales	$10,000
2	Volume Increase %	1%	x	Annualized Sales x GPM	$6,000
3	COGS Reduction %	1%	x	Annualized COGS	$4,000
4	Overhead Reduction %	1%	x	Annualized Overhead	$4,500
5	DSO Reduction Days	1	x	Annualized Sales/360	$2,778
6	DII Reduction Days	1	x	Annualized COGS/360	$1,111
7	DPO Increase Days	1	x	Annualized Purchases/360	$1,111
				TOTAL ANNUAL IMPACT ON CASH FLOW:	$29,500 2.95% of Sales

Assumptions		
Sales	1,000,000	100%
COGS	400,000	40%
Gross Profit	600,000	60%
Overhead	450,000	45%
Net Income	150,000	15%