



Maximize Your Working Capital

The drastic downturn in the subprime mortgage market and the resulting credit crunch and housing crisis have dominated recent news headlines. The economic slowdown and potential for recession have been hotly debated by financial analysts, and Congress and the Department of the U.S. Treasury are discussing how best to reduce foreclosures.

By Ed Haidenthaler

As banks that lend money in various segments of the market take losses on their mortgage portfolios, they tighten the terms and availability of funds for other forms of loans. Some of the funds affected by this tightening are accounts receivable financing and working capital loans.

In today's tough credit environment, a company may not be able to get the bridge loans the finance department relies on for working capital or the loans may be too costly. This means that companies of any size in any industry are looking for ways to maximize their working capital and minimize the day-to-day impact of the credit crunch.

The old adage "cash is king" really is true, especially when credit is tight. When cash is short, many companies start cutting expenses. Unfortunately, there are only so many expenses that can be cut before the company's ability to maintain growth and healthy operations is compromised.

Cash Management Options

Working capital optimization must be a companywide initiative to realize a measurable impact, and cutting expenses is only one part of the cash equation. The other part is cash management. It deals with operations, and includes a company's product or service development and sales cycle. For example, sales personnel can restrict the payment terms they grant in selling the products or services. Raw materials and purchasing pipelines can be shortened so costs of goods can be reduced or are better timed with manufacturing and sales. Accounts receivable can be more closely monitored to shorten average days outstanding on sales and increase collection percentages. Accounts payable teams can determine if paying bills early to take advantage of payment discount terms adds value when compared with the company's cost of cash. And, of course, every department should re-evaluate its own processes to encourage efficiencies and cost-cutting.

For cash management to be effective, compensation must be tied to a specific cash management strategy to drive the culture shift. Sales staff should not only be paid as a result of sales transactions, but also have a stake in the collection and restriction of sales credit terms. Raw materials managers and purchasing staff should have a portion of their compensation tied to the goals of reducing lead time and creating just-in-time inventory management. Accounts payable staff should be compensated in part by their ability to lengthen or manage payables. Likewise, accounts receivable staff, as well as sales staff, should be compensated in part for their ability to collect more and reduce write-offs. Finally, all personnel should be rewarded for expense management and cost-cutting, which may even include a savings sharing plan.

Working capital is a primary indicator of a company's financial health. Positive working capital enables companies to meet current and long-term financial obligations. If the entire organization is cash-management oriented — not only in strategic planning, but also in compensation — then the whole firm will be better positioned to weather the storm of the credit crunch. ●

Ed Haidenthaler, director of finance and accounting for the Salt Lake City office of Jefferson Wells, can be reached at ed_haidenthaler@jeffersonwells.com.