Forecasting Cash Flow

by Linda Case

If you were to chart cash on hand alongside profits, you would find that their cycles are quite different. A heavy volume of work over a period of several months may produce good profits, but you need lots of cash to pay for materials, labor, and subs. Often, draws do not keep up with expenditures, so despite the profitable work, your bank account is low. The reverse is also true. A string of high-volume months may be followed by a slow period, but because you're still collecting payments from earlier work, your bank account is flush.

Running your company by reacting to the ebb and flow of cash is a quick road to disaster. Only a Profit and Loss statement can tell you what your true profits are. But you must be aware of cash as well. Not having enough cash at the proper time has been the death knell to many a profitable remodeling company.

Monitoring Cash Flow

It's difficult in remodeling to project cash flow accurately over a long period of time. After all, you may not yet know about a job you may be collecting money from in three months. It can be helpful, however, to project short-term cash flow — one month or even one week at a time. The ability to forecast may help you solve oncoming cash flow problems. Based on your projections, for example, you may decide to speed up work on a job to collect a large draw sooner. Or you may decide to hold off on purchasing new equipment.

Consider using a Cash Flow Projector form to predict your cash position (see sample form). If you are profitable over a period of time, you should be able to build up a cash reserve that reduces cash shortfalls and make your business life less stressful.

Improving Cash Flow

Yet even the most successful business has some periods during the year when cash must be hoarded and carefully doled out. Follow these 15 tips to create a more favorable cash flow.

1. Draw at "start," not "completion." If you use draws based on job progress, always arrange for payment to become due upon the start of a phase rather than at its completion. You will maximize your cash and minimize your arguments with the customer. You don't have to change the timing of the draw; for example, just substitute "upon start of trim" for "upon completion of drywall."

2. Big first draw. Collect a first draw that is fair to the buyer but gives you as much leverage as possible. If state law permits, ask for as much as 30% down on mid-sized jobs, 50% with small jobs. If the job is particularly material heavy, consider a larger first draw. For example, collect 50% of the contract before commencing a kitchen remodel to compensate for the large volume of special materials that must be ordered.

3. Split the final draw. Create two draws instead of one. The first should be larger and due at substantial completion (when the space is ready for occupancy); the smaller draw, upon completion of the punch list. Don't let other charges — like change orders, selections, and time-and-materials work — fall into the final draws. Be sure to bill them as early as possible.

4. Collect at regular intervals. Some remodelers have been successful using draws based on a time period. They may collect every week or every two weeks. For example, if the $12,000 Basehart job is expected to take six weeks, collect $2,000 a week. If there is a delay, adjust the draw schedule.

5. Request a retainer. An increasing number of remodelers who work on a cost-plus or time-and-materials basis are requesting a substantial "retainer" before they begin the job.

6. Collect in person. Hand-deliver invoices and personally pick up checks. Over a year's period, this practice will make major inroads on cash flow problems.

7. Personalize bill collecting. When a client is slow to pay, don't just send additional invoices. Discuss the problem by phone or meet with the customers in person to settle any confusion and answer questions.

8. Commercial jobs need extra effort. When doing work for another business, such as commercial work or insurance reconstruction, find out at the contract signing who will approve bills and pay them, and ask about the firm's payment procedures. Different offices may have to approve an invoice before it is paid, or an invoice may need two or more signatures. If you know the system, you'll get paid faster. Faxing two invoices may help: one for the person supervising construction and one for the person actually approving payments.

9. Take your discounts. Always pay discounted bills in time to take the discount. The percentage you save for spending your money 20 days earlier is a bargain. Pay other bills on the last date that will maintain your company's good credit.

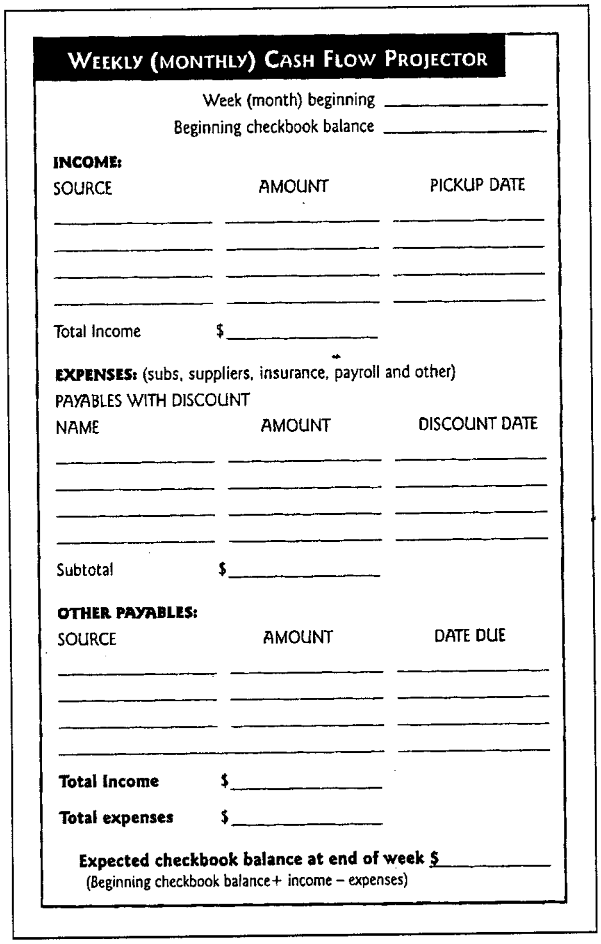
10. Subcontract rather than employ. Subcontractors are often paid only once or twice during a job, whereas your own labor may be paid each week.

11. Use credit cards. Rather than purchasing in cash or on account, use credit cards that give you a rebate or airline mileage. This will extend credit to your company for a month or so interest-free, providing you pay the charges off monthly. However, don't let this get out of hand and get you into debt. Interest on late payments is steep.

12. Open charge accounts. If you don't have open accounts with all of your suppliers, see if you are eligible for them. A monthly account may save you money through both the extended credit and the available discounts.

13. Consider a biweekly payroll. You'll increase your cash flow while cutting the cost of doing payroll in half. Thousands of remodelers have accomplished this successfully and, yes, field personnel can make the adjustment.

14. Open a line of credit. As your volume gets larger, you may want to develop a line of credit with a bank that can be used to smooth out the firm's cash needs. Think of a line of credit only as a short-term bridge loan — not a way to get out of financial trouble, but a means of taking work that requires you to temporarily finance the job. Be sure to pay up your line of credit once a year.



WEEKLY (MONTHLY) CASH FLOW PROJECTOR

Week (month) beginning ____________

Beginning checkbook balance ____________

INCOME:

SOURCE	AMOUNT	PICKUP DATE

Total Income $____________

EXPENSES: (subs, suppliers, insurance, payroll and other)

PAYABLES WITH DISCOUNT

NAME	AMOUNT	DISCOUNT DATE

Subtotal $____________

OTHER PAYABLES:

SOURCE	AMOUNT	DATE DUE

Total Income $____________

Total expenses $____________

Expected checkbook balance at end of week $____________

(Beginning checkbook balance + income – expenses)

Head off cash shortages by tracking income and expenses weekly on a simple form. This short-term forecasting will help you decide when to delay purchases or speed up the pace of work to accelerate payment schedules.

15. Watch warehousing. Inventory ties up cash. The savings from buying in quantity and stocking frequently used materials may not make up for the cost of space, keeping inventory records, and tracking damage to stored materials.

Cash flow can be your friend or your foe. I've seen remodeling businesses devastated by lack of cash. The owner's focus becomes robbing Peter to pay Paul instead of running an effective business. However, if you are currently running your company with a loss, let me cheer you by telling you that I've also seen remodelers make striking comebacks with the help of excellent money management.

Adapted from The Remodeler's Guide to Making and Managing Money, *written by **Linda Case** and published by Remodeling Consulting Services of Silver Spring, Md., of which she is the founder.*