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STRATEGIES FOR ENHANCING A COMPANY'S CASH FLOW

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Abstract

The flow of money into and out of the company is the focus of the cash flow statement. At the operational, investing, and financing activity level, it displays a company's liquidity situation and the impact of changes to the balance sheet and profit and loss account on cash and cash equivalents. To increase cash flow, a corporation must implement a number of strategies, such as enhancing the debtor-creditor cycle, factoring, discounting letters of credit, accepting advance payments, and more.

Keywords: Cash Flow, Financial Management, Accounting Standard 3.

Introduction

Every business depends on cash flow, which is also the main sign of a healthy company. The Statement of Cash Flow is another name for cash flow in financial accounting. Your cash inflow will always exceed your cash spending throughout a perfect company cycle. In a straightforward experiment, having enough cash on hand to pay creditors on time is a sign of healthy cash flow. However, when businesses are unable to achieve this, they experience "cash crises," which lead to the collapse of their organization. An outstanding staff is necessary to handle cash flow effectively and overcome such issues. When access to liquidity is limited due to a credit crisis, cash management becomes essential to survival. Cash flow has a real, immediate, and, if poorly managed, completely harsh influence.

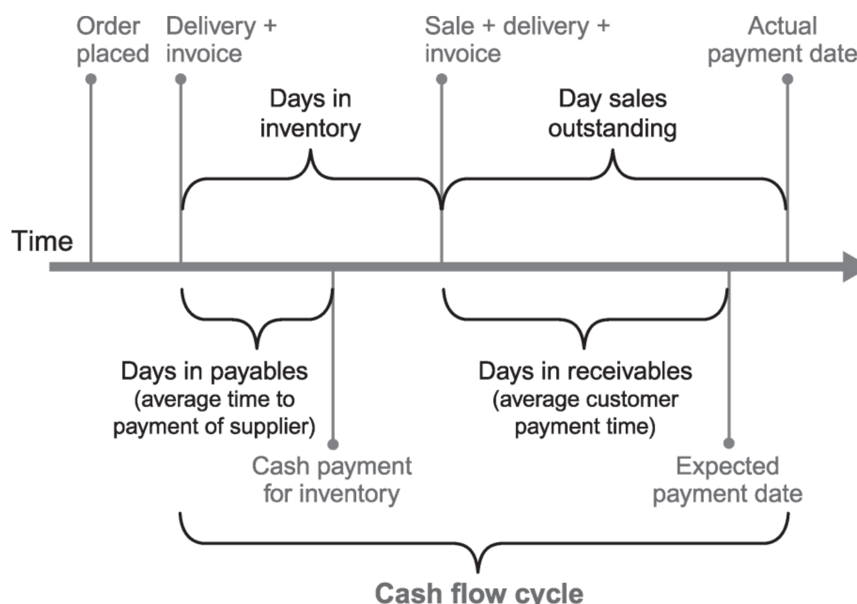
Objectives of the Study

1. To recognize the cycle and significance of cash flow in a company.

Cash Flow Cycle

The third Indian Accounting Standard addresses financial flow. Cash flow can be defined as a cycle in the context of finance. Cash is used by every company unit to purchase resources, pay for normal expenses, pay for unpaid bills, and buy materials, among other things. Every resource is used to produce commodities and services. The cycle then repeats itself once they are sold to clients, payments are received, and the money is once more invested in additional resources. Actively managing and controlling these cash inflows and outflows is vital for any company organization.

Inflow (money coming to the business)	Outflow (money we pay out)
Money received from sale of goods and services to customer	Purchase of raw material for production
Account receivable	Acquisition of production-related raw materials
Bank Loan	Purchasing fixed assets
Interest received on investment	Paying salary and wages
Investment by shareholder in the company, etc	Making loan principle and interest payments Tax obligation, etc.



Advantages of Managing a Good Cash Flow

1. Liquidity

Solve the liquidity issue as much as possible with sufficient cash on hand or in the bank. Such surplus enhances the company's creditworthiness and is essential in obtaining pricing benefits from creditors.

2. Productivity

Controlling cash flow makes it simple to handle financial activities, including accounts receivable, bank interest, principal loan repayment on time, and so on. This allows management to concentrate on the productivity of the firm and its commercial advancements.

3. Re-invest in the Business

A better cash flow might assist the organization in reinvesting its earnings. To increase our company's productivity, profitability, and competitiveness, we can use this money to develop new facilities, hire additional staff, extend our current assets, and invest in new technologies and procedures.

4. Reduce Debt

When we have extra money, we can pay off debt, which lowers monthly expenses like high interest rates and even late fees.

5. Peace of Mind

The ability of management to manage efficient cash flow is a constant source of stress in any organization. However, if the business has excess cash flow, it undoubtedly gives management piece of mind, enabling them to be prepared for any opportunities or difficulties that may arise in the future.

Ratios

When analyzing a company's financial data, ratios are vital. A healthy cash flow cycle is maintained by the use of a number of ratios.

Current Ratio

Low Risk	Average Risk	High Risk
Over 1.5	1.0-1.5	Under 1.0

Liquidity Ratio

Low Risk	Average Risk	High Risk
Over 1.25	0.75-0.25	Under 0.75

ROCE (Return on Capital Employed)

Low Return	Average Return	High Return
Under 6%	8-11%	Over 11%

Debt/Equity (Gearing)

The aim of this ratio to find out how heavily the company is relying on external funding to support the business.

Low	Average	High
Under 50%	50-90%	Over 90%

Debt (loan overdraft etc.) dividing by equity (shareholder fund) x 100

An alternative definition is debt divided by (debt plus equity), which would modify the above table:

Low	Average	High

Under 33%	33-47%	Over 47%

Profit/Sales Ratio

Low	Average	High
Under 3%	3-10%	Over 10%

Debtor's Days Sales outstanding

Low	Average	High
Under 55 days	55-85 days	Over 85 days

Creditors Days Sales

Low	Average	High
Under 45 days	45-60 days	Over 60 days

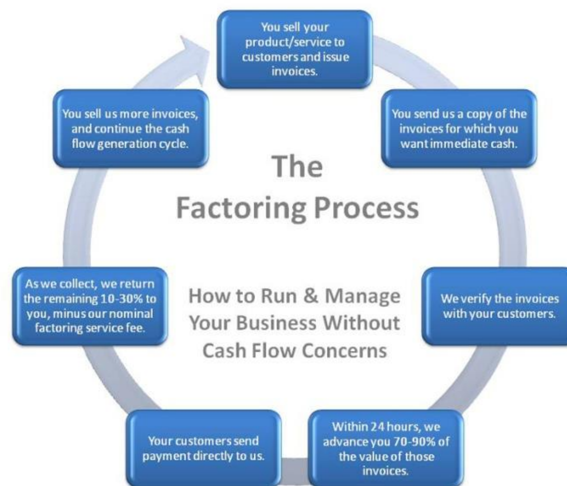
Sources to Improve Cash Flow

The important key elements to improve effective cash flow are as follows.

Factoring

One financial solution for managing receivables and enhancing the cash flow cycle is factoring. Factoring is the process of turning credit sales into cash for a brief time frame, such as 15, 30, 60, 90 days, or up to the authorized trade cycle. In factoring, a financial institution (the factor) purchases a company's (the client's) accounts receivable and pays up to 70% to 90% of the invoice value right away. When the factor receives 100% of the money from the client's debtors on the due date, the factoring business pays the remaining 10% to 30% to the customer (after subtracting financing costs, such as interest costs, invoice handling fees, and service tax).

Factoring Works



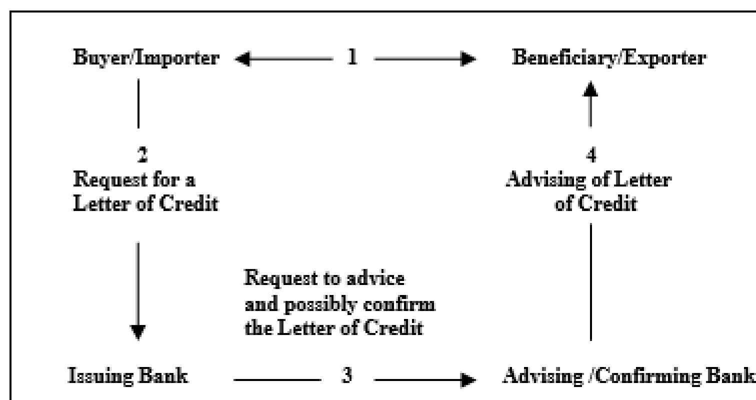
Advantages of Factoring

Factoring has many benefits, some of the more significant of which are listed below:
1. Beneficial for setting up quick, short-term financing.
2. Beneficial for cutting operating costs.
3. Efficient cash flow and faster working capital access.
4. Improved solvency, creditworthiness, and financial standing.
5. Factoring is useful for increasing the balance sheet's potential.

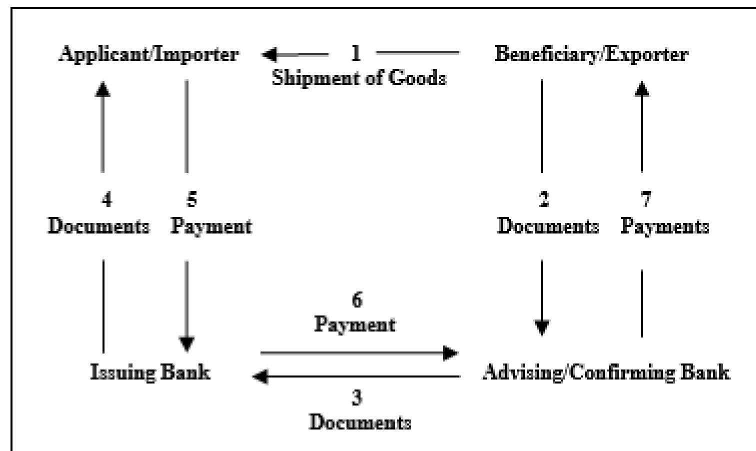
Letter of Credit (LC)

A commercial document called a letter of credit is useful for keeping a healthy cash flow cycle. Because a bank issues it in the regular course of business and is obligated to guarantee payment in the event of an unfavourable circumstance. A bank will grant LC to a third party (beneficiary) at the client's request. It is an essential instrument insofar as it streamlines and secures transactions, guaranteeing the party to whom the LC is opened that, in the event of a bad circumstance and the client fails to make the payment, the issuing bank will make the payment in accordance with the terms and conditions specified at the time the LC was issued. When both parties are conducting business for the first time, this paper is significant. Because the bank guarantees the safety of both parties participating in the transaction, these parties can conduct business with little to no risk.

Issuance of Letter of Credit



Payment under Letter of Credit



Handling Receivables (Debtors)

Receivables have an importance to a company's ability to sustain efficient cash flow. Businesses suffer greatly when payments are delayed, especially small and medium-sized businesses. The actions listed below will assist you in managing your debtors:

1. Maintain the proper mindset when it comes to credit management and ensure that it receives the attention it merits.
2. Make it a corporate policy to establish transparent credit processes.
3. Ensure that employees, vendors, and clients are aware of these procedures.
4. When taking on new accounts, especially bigger ones, act professionally.
5. Before granting credit, properly examine each client. Make use of industry sources, bank references, credit agencies, etc.
6. Set and adhere to credit limitations for every client.
7. If you anticipate difficult times ahead or work in a risky industry, keep an eye on these boundaries.
8. Stay in close proximity to your biggest clients.
9. Take into account assessing penalties for past-due accounts.
10. Take into account allowing credit and debit cards as a form of payment.
11. Keep an eye on the aging schedules and debtor balances; avoid allowing any loans to get too big or too old.

Managing Payables (Creditors)

A company's ability to sustain efficient cash flow depends on its ability to manage its creditors. Cash outflows are caused by improper or inappropriately timed purchases, and liquidity issues might arise from an overly enthusiastic purchasing function. The actions listed below will assist you in managing your creditors:

1. Preserving positive credit relationships with vendors.
2. Who in your organization has the authority to make purchases? Is it centralized or delegated to several (younger) individuals?
3. Are purchase amounts adjusted to account for anticipated demand?

4. Do you employ order quantities that account for purchasing and stock-holding expenses?
5. Are you aware of how much carrying stock costs the business?
6. Do you have any other supply sources? If not, obtain quotes from significant vendors and compare prices and terms of financing to lessen reliance on one source.
7. What percentage of your vendors offer a return policy?
8. Can you swiftly raise prices for your clients in order to cover cost increases?
9. Can you repay the cost of the delay if a supplier of products or services fails to meet your expectations?
10. Is it possible to confidently set up just-in-time or staggered supply deliveries?

In business, it's said that if you can buy well, you can sell well. Managing your suppliers and creditors is equally important as managing your debtors. It's essential to take care of your creditors; failing to make payments on time could promote anger and give the impression that your business is ineffective (or in in danger!). Therefore, the business must take the necessary steps to manage its creditors' cycle effectively. If this is done, it will undoubtedly help manage the cash flow cycle effectively.

Inventory Management

Inventory management is a balancing act. A company's cash resources may be severely strained by excessive inventory, while a shortage of inventory may lead to missed sales, client delays, etc. Knowing how quickly your entire stock is moving or, to put it another way, how long each item of stock sits on shelves before being sold is vital to inventory management. Naturally, the type of firm will have an impact on average stock-holding durations. A fresh vegetable store, for instance, might rotate all of its inventory every few days, but a motor factor would operate considerably more slowly since it might keep a large inventory of little used spare parts in case someone needed them. The following actions should be taken in order to manage an inventory cycle effectively:

1. Examine how well the current inventory and purchasing systems are working.
2. Be aware of the stock turnover for each of the main inventory items.
3. Simplify controls for the insignificant many while imposing strict controls on the important few.
4. Get rid of slow-moving or outmoded items; the longer you hold onto them, the harder it will be to sell.
5. Rather than producing your own goods, think about outsourcing a portion of it to another company.
6. Verify that no merchandise "is going out the back door!" by reviewing your security protocols.

Pricing Discounts

This solution proves essential for rapidly improving the cash flow cycle of the business. It entails offering your clients discounts in exchange for early payment. By encouraging clients to pay before the usual billing cycle, this strategy may improve cash flow

management even though it may have an adverse effect on your profit margin. This can also be used by your business to take advantage of suppliers and other people you owe money to, but be careful that paying off debt early doesn't leave you with a cash flow deficit.

Equity Financing

A business can use debt, equity, or both to fund its operations. Equity finance refers to money invested in the company, either by the owner or by one or more investors. The primary benefit of equity financing for the business is the reduction of interest expenses, which enhances the cash flow cycle. In this instance, investors invest money in a business with the expectation that they would profit from it and that the stock will increase in value. Of course, they can receive dividends (their portion of the profit), but only by selling the stock can they regain its value.

Conclusion

A cash flow statement can be used by a business to predict future cash flow, that supports with budgetary issues. Whether a company is financially sound or not is determined by its cash flow, which investors use to evaluate its health. If the company is not financially sound, an efficient cash flow cycle must be maintained. According to what I understand, I have included all the essential components in this post that are essential to enhancing the cash flow cycle. If a business adopts this approach, it will undoubtedly never experience cash flow issues.

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