

Effective Cash Flow Management

by David Hetherington

Managing a company's financial health requires time and consistent diligence, with the task taking on more complexity as the organization scales up. Whether your publishing business is a startup or an established enterprise, there are three financial tools that are fundamental to assessing the ongoing health of the organization:

1. **Income Statement:** Sometimes referred to as the profit-and-loss statement, this report details the profit or loss performance of the business and, at its most basic, is calculated by the simple equation $\text{Sales} - \text{Expenses} = \text{Net Income}$. The elements included in the income statement will vary depending on whether the enterprise is recording performance on the cash or accrual method.
2. **Balance Sheet:** The balance sheet details the financial position of the company on a specific date and consists of the organization's assets (what the organization owns), its liabilities (what the organization owes to third parties), and the owner's equity, which is the difference between the assets and liabilities and reflects the owner's share of the business.
3. **Cash Flow Statement:** The cash flow statement is a summary of the cash inflows and outflows of the business and, in many ways, is the most important of the three financial statements because it serves as a barometer of the enterprise's ability to fund day-to-day operations. The primary reason businesses fail is the lack of the requisite funding or the working capital necessary to fund day-to-day operations, including payroll, fixed and overhead expenses such as rent, and ensuring that vendors are paid on time.

These three financial statements are common to all businesses, but in terms of cash management, few industries face the challenges of book publishing—with its notoriously extended payment cycle for accounts

receivables of 90 to 120 days, the very real risk of payment with returns instead of cash, deep discounts required by channel partners, and the not unreasonable expectation that the printers providing publishers with inventory will be paid in 30 days, and 60 at most.

Day-to-day survival hinges on closely monitoring cash needs. That means knowing when and how much cash will come in from partners, and when it must go out for payroll, expenses, inventory, and royalties. Ignoring these inflows and outflows invites financial trouble.

Creating a cash receipts and disbursements schedule is essential to the health of the business, but even more critical is maintaining the cash management discipline needed to navigate the inevitable peaks and valleys of publishing. Business expenses are paid with cash in the bank—not profits on an income statement. Profitable companies run out of cash all the time, while unprofitable ones can survive for years if they maintain enough liquidity to meet financial obligations.

Regardless of the size of the publishing business, there are several steps that organizations can take to strengthen their cash position and reduce the risk of running out of cash (and bankruptcy). Following is a list of proven strategies to optimize your cash position:

- **Understand Your Cash Flow Cycle:** At minimum, you should build a spreadsheet that maps out the receipt and disbursement of cash by major operating categories, including revenues and expenses, including (but not limited to) inventory investment and royalty payments and considers non-operating sources of cash such as lines of credit.
- **Update Your Forecast Regularly:** The model should receive constant attention to ensure that you are not overlooking important developments, particularly significant delays in collecting receivables or returns surges submitted instead of cash.
- **Improve Receivables Management and Monitor Returns:** Both activities should be managed at the customer level. Re-evaluate your relationship with customers who are consistently and significantly

late in making payments and/or have high returns. Some sales are not worth having if they place your business at risk.

- **Extend Payables Prudently:** If you can trade price for payment terms, you should give it close consideration.
- **Review Profitability by Product Line, Distribution Channel, and Trading Partner:** While diversification is certainly important to minimize risk and optimize growth opportunities, you should understand the costs and benefits of all your business partners and products.
- **Optimize Inventory:** Think digital short run manufacturing versus offset to minimize your inventory investment and obsolescence risk. As an industry, we often suffer from more optimism about the expected success of our projects than might be warranted. In the case of inventory, less is often more.
- **Reduce Fixed Costs and Transition to a Volume-Driven Variable Cost Model:** This is especially important in an environment with a high degree of market uncertainty.
- **Invest Cautiously in Growth:** Expansion of your business by organic growth and/or acquisition is certainly a desirable outcome, but growth that puts unexpected demands on your cash reserves may cause more harm than good unless managed carefully.
- **Adopt Zero-Based Budgeting:** Your annual budget should be built from the ground up each fiscal year. The budgeting process should include a top-to-bottom review of all the elements in your income statement and a comprehensive evaluation of the implications for cash flow.
- **Cultivate Banking Relationships in Advance:** Your financial planning should include establishing a line of credit in advance sufficient to fund short-term cash needs in those inevitable situations where incoming cash from operations is insufficient to fund the demands for outgoing cash. The line of credit should be secured before you need it, and it will be easier to secure if your cash flow projections demonstrate the business's ability to service debt.
- **Build Your B2C and B2B e-Commerce Capabilities:** Recapture a portion of the margin given to channel partners through discounts and commercial terms. Build long-term customer relationships through the sale of e-books and physical books. E-commerce

typically translates to the immediate receipt of cash, significant improvement in margin, and the development of communities that add long-term value to the firm.

- **Educate Your Team:** Managing cash requires that you and your team understand the role each plays in the effective management of cash.

Building a successful publishing business is a daunting enterprise under the best of circumstances, and success and failure are often separated by a fine line. While product quality and a sound sales and marketing strategy are unquestionably of paramount importance, the less glamorous day-to-day attention to the financial health of the business may well make the difference between “the thrill of victory and the agony of defeat.” •



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