



Revenue is Vanity, Profit is Sanity, Cash Flow is King

Alan Miltz
Founder Cash Flow Story
Chairman Pearl Financial Services
Co-author Scaling Up



Contact Details

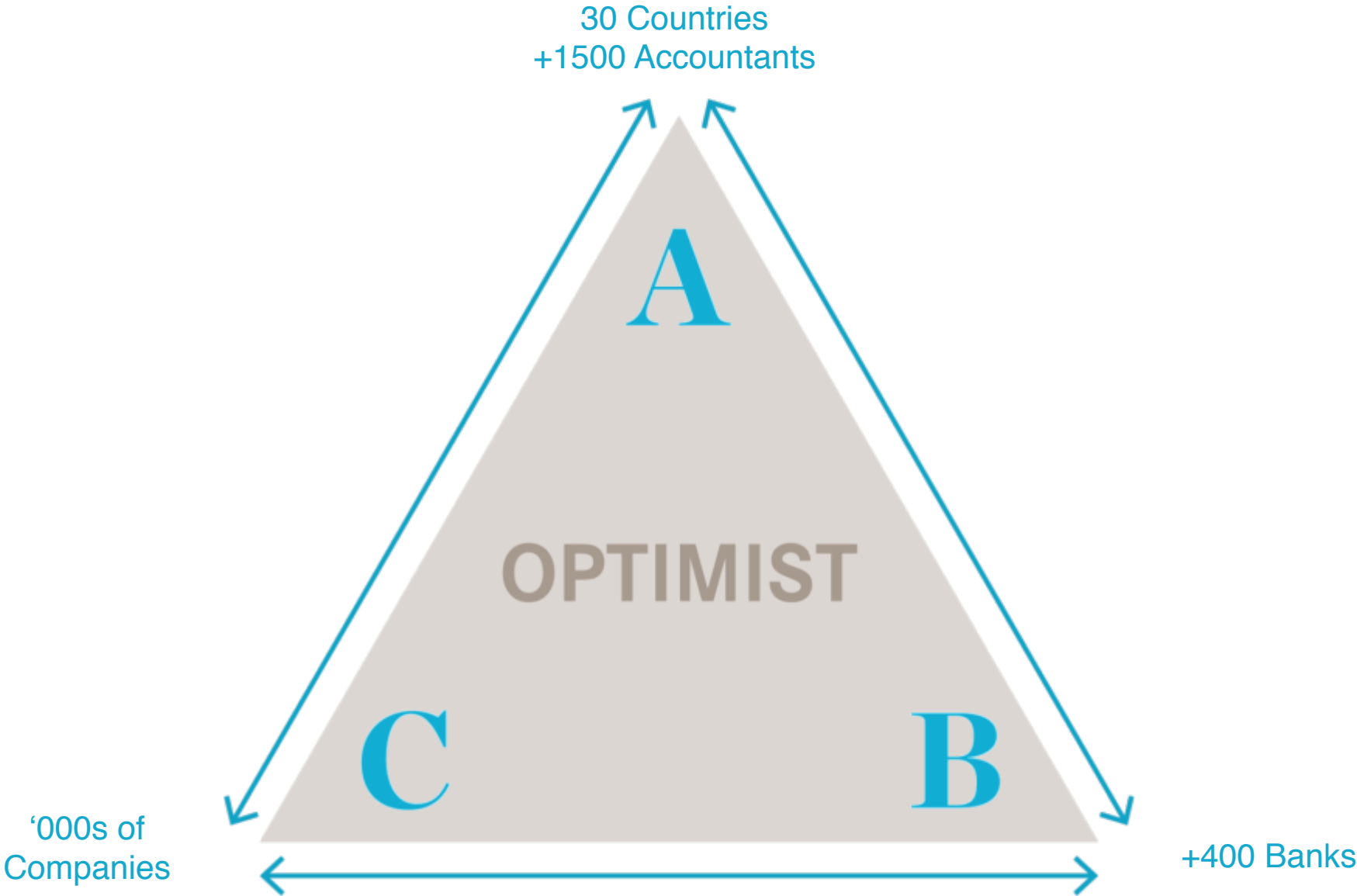
Email: alan.miltz@pearlfinance.com.au

Phone: +61412300401

Website: www.cashflowstory.com

A video summary of this course can be found at
www.cashflowstory.com/resources

Notes available at:-
<http://cashflowstory.com/exclusive>





What you will learn:

- How to implement cash flow story in your business

**One page
financial
scorecard**

**The 4
chapters**

**The 3 big
Cash Flow
Measures**

**The
Power of
one**

**Cash flow
quality**

**Business
value
indicator**

- How banks review your business
- Monthly management meeting



8 keys to business success:

- Two heads are better than one
- Everyone has the right to be heard in a non-threatening way
- The truth will be told
- Our word is our bond
- The needs of the customer come first
- There will be no surprises – put the uncomfortable issues on the table
- Promote teamwork and leadership
- Be proactive corporate citizens





5 success factors

1. If you aim for the moon you might make the sky, keep trying.
2. Write things down in Black and White (The Dream) Business Plan
3. Get the right people into the Organisation, the backbone people not the high flyers
4. Hard work - No substitute for hard work and persistence, never give up
5. Always back your own judgement



Case Study: William's Plumbing Products

- William's Plumbing Products was founded in 2001
- William's is an importer of plumbing products and distributes to building sites, major construction projects and hardware stores.
- William's believes they are doing fantastically
- Current facilities are a trade finance, overdraft and a long term facility secured by internal and external property

Case Study: William's Plumbing Products

Profit & Loss	2015	2016
Revenue	35,000,000	42,000,000
Gross margin	10,500,000	13,020,000
Overheads	6,751,140	8,401,150
EBIT	3,748,860	4,618,850
Interest	1,165,900	1,363,480
Tax	930,280	1,172,348
Net profit	1,652,680	2,083,022

Balance Sheet	2015	2016
Cash at bank	0	0
Accounts receivable	6,712,330	8,630,137
Inventory	10,336,960	14,291,507
Current assets	17,049,290	22,921,644
Fixed assets	8,500,000	9,500,000
Total assets	25,549,290	32,421,644
Accounts payable	4,028,550	5,557,808
Short term debt	5,019,740	7,279,813
Current liabilities	9,048,290	12,837,621
Long term debt	9,000,000	10,000,000
Total liabilities	18,048,290	22,837,621
Share capital	2,001,000	2,001,000
Retained earnings	5,500,000	7,583,022
Total liabs & equity	25,549,290	32,421,644



Case Study: William's Plumbing Products

- On a scale of 1 to 10 how would you rate William's Plumbing Products financial performance?
- On a Scale of 1 to 10 how do you think the Bank rates William's Plumbing Products financial performance?
- What is William's cash flow for 2016?



Net cash flow:

- On the 1st of January 2015 I have \$10,000 in the bank.
- On the 31st of December 2015 I have \$1,000 in the bank.

“What is my net cash flow?”





Net cash flow:

Why can't we apply this logic to the company?



William's net cash flow:

Opening net debt

Cash at Bank	Nil
Short term debt	5,019,740
Long term debt	9,000,000

14,019,740

Closing net debt

Cash at Bank	Nil
Short term debt	7,279,813
Long term debt	10,000,000

17,279,813

Net cash flow	-3,260,073
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The four chapters

- Chapter 1 - Profitability
- Chapter 2 - Working Capital
- Chapter 3 - Other Capital
- Chapter 4 - Funding and Returns

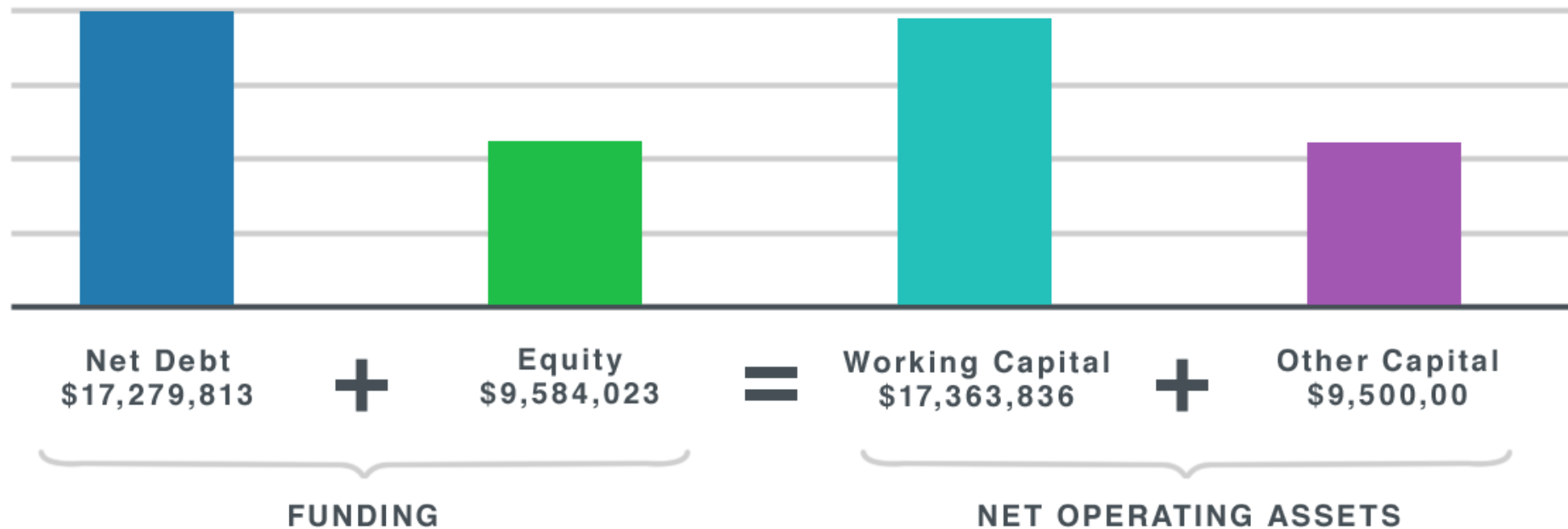


Reconciliation of Cash using the 4 Chapters

	+ Cash Flow	- Cash Flow
Chapter 1 - Profit	2,083,022	
Chapter 2 - Working Capital		-4,343,096
Chapter 3 - Other Capital		-1,000,000
Total	2,083,022	-5,343,096

The business needed \$3,260,073 of borrowings to fund the gap

Your Balance Sheet in one Sentence

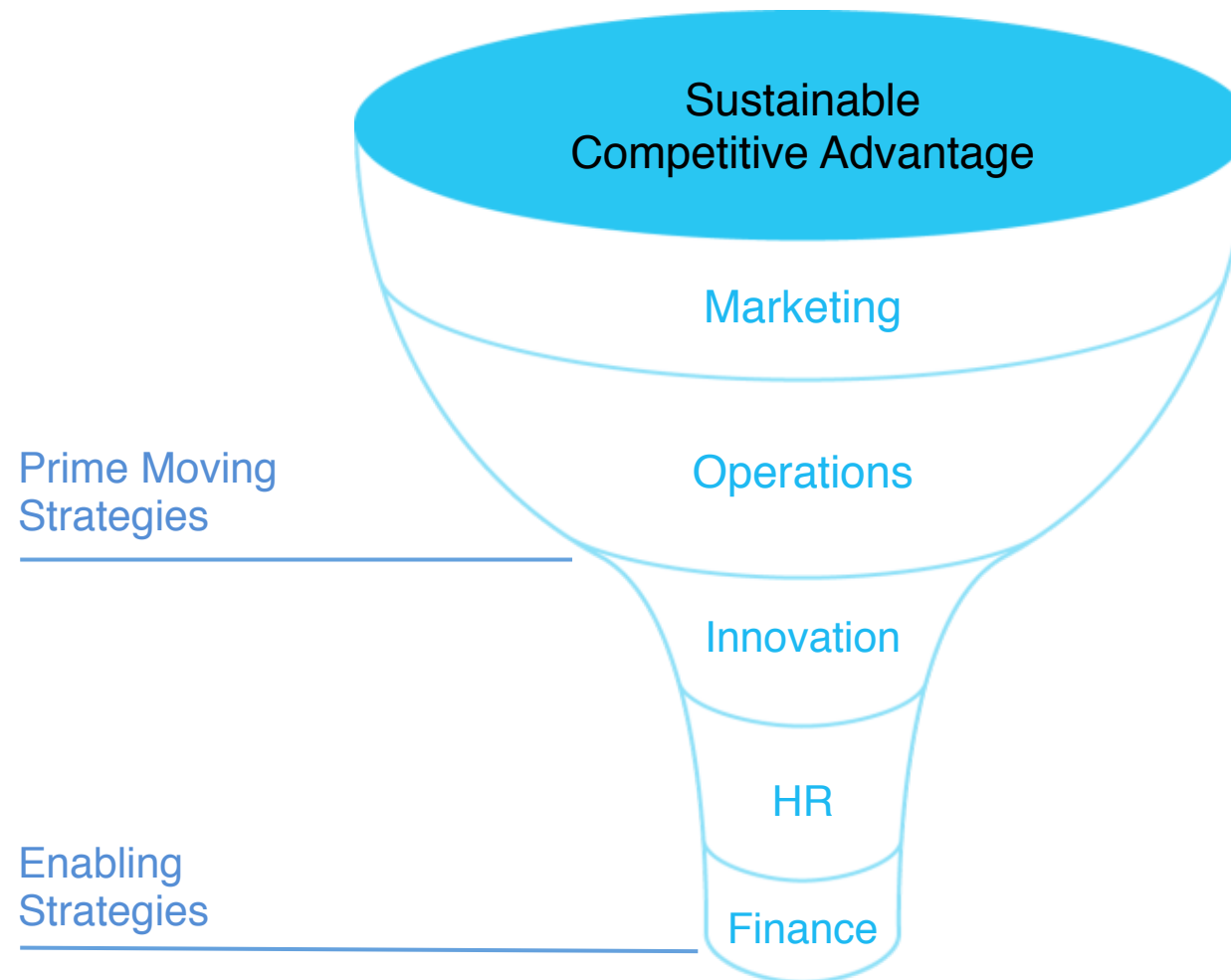




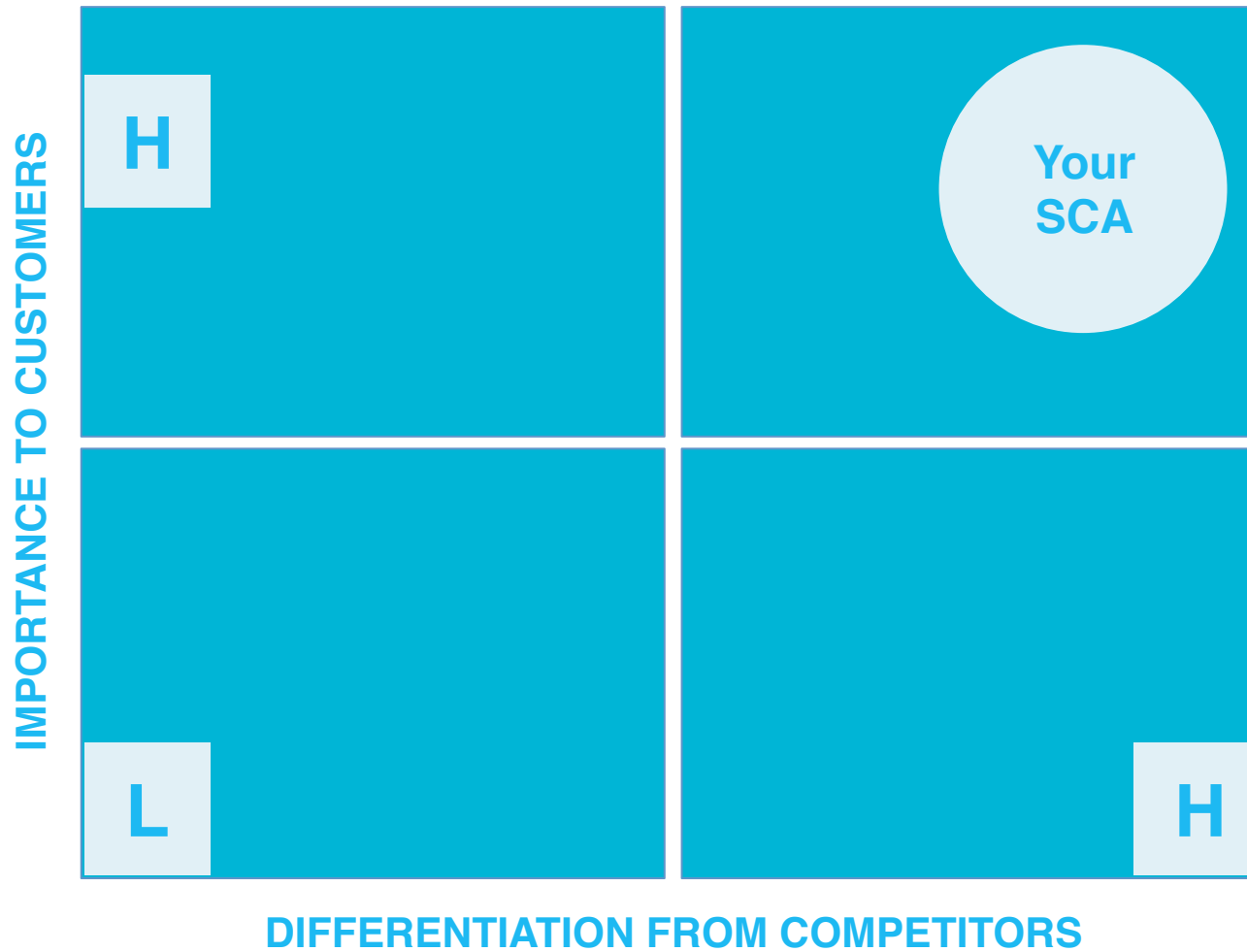
Your Balance Sheet in one Sentence

Equity	Net Debt	=	CA	NCA	CL	NCL
9.5	17.3					
		AR	8.6			
		Inv	14.3			
		AP			(5.6)	
		FA		9.5		

The Funnel Analogy:



Plotting your Critical Success Factors





How does finance measure your SCA?

- Profit?
- Revenue Growth?
- Cash Flow?
- Market Share?
- Return?
- Dividends?



How does finance measure your SCA?

The four chapters

- Chapter 1 – Profitability
- Chapter 2 - Working Capital
- Chapter 3 - Other Capital
- Chapter 4 – Funding and Returns



Why go into business?

Return On Capital Employed (ROCE)

or

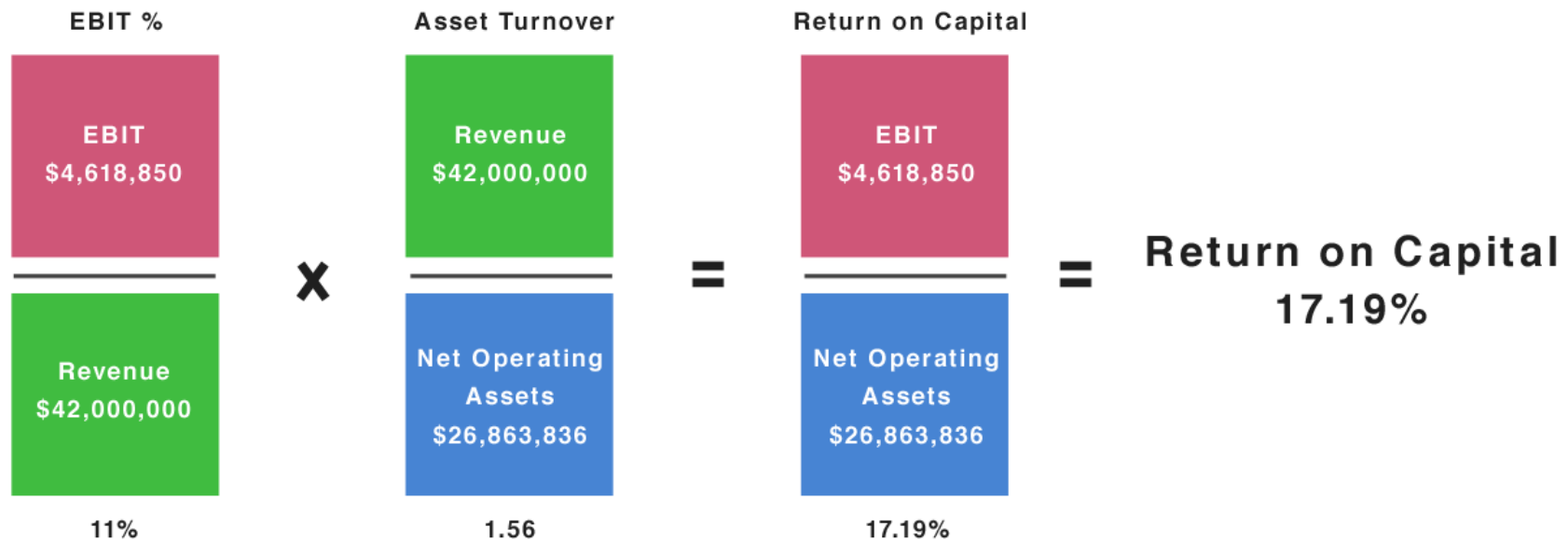
Return On Net Assets (RONA)

ROCE = RONA

(the DuPont Theory of Financial Analysis)

Financial analysis – the theory

$$\text{ROCE} = \text{EBIT} / \text{Net Operation Assets}$$



The ROCE Equation:

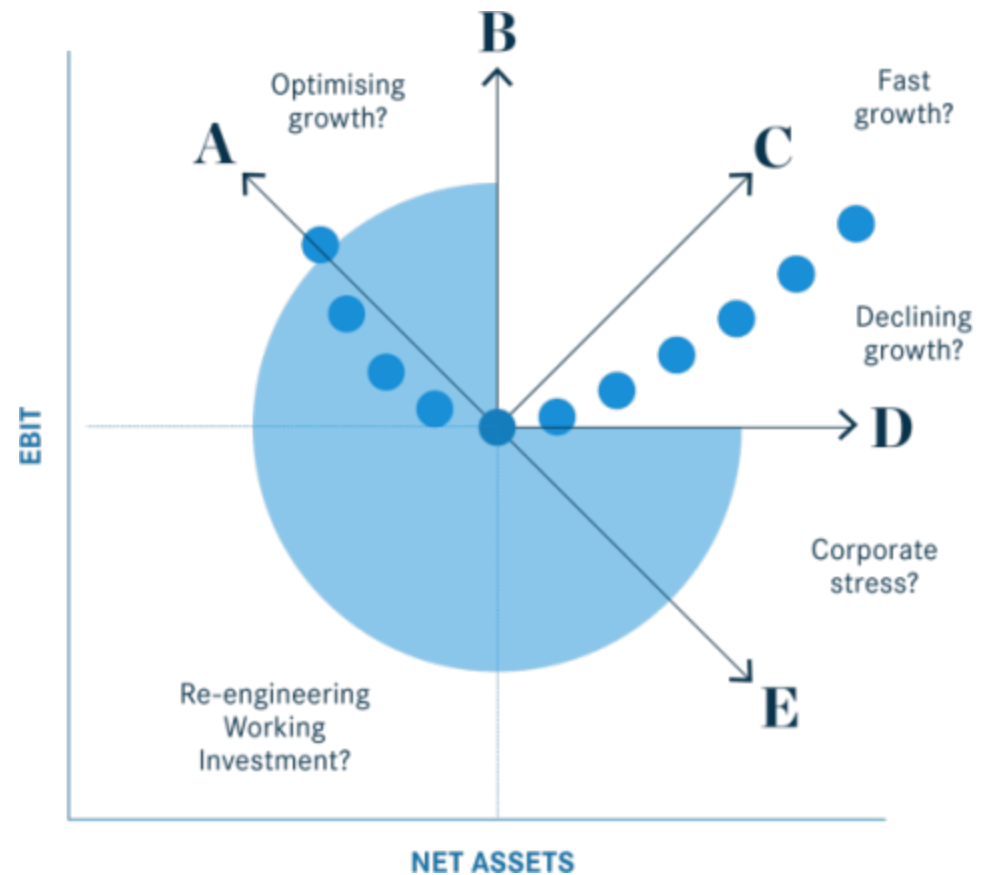
As management it is mission critical that over time we ensure that our EBIT is growing at a faster rate than our investment in our Net Operating Assets.



Optimizing Growth

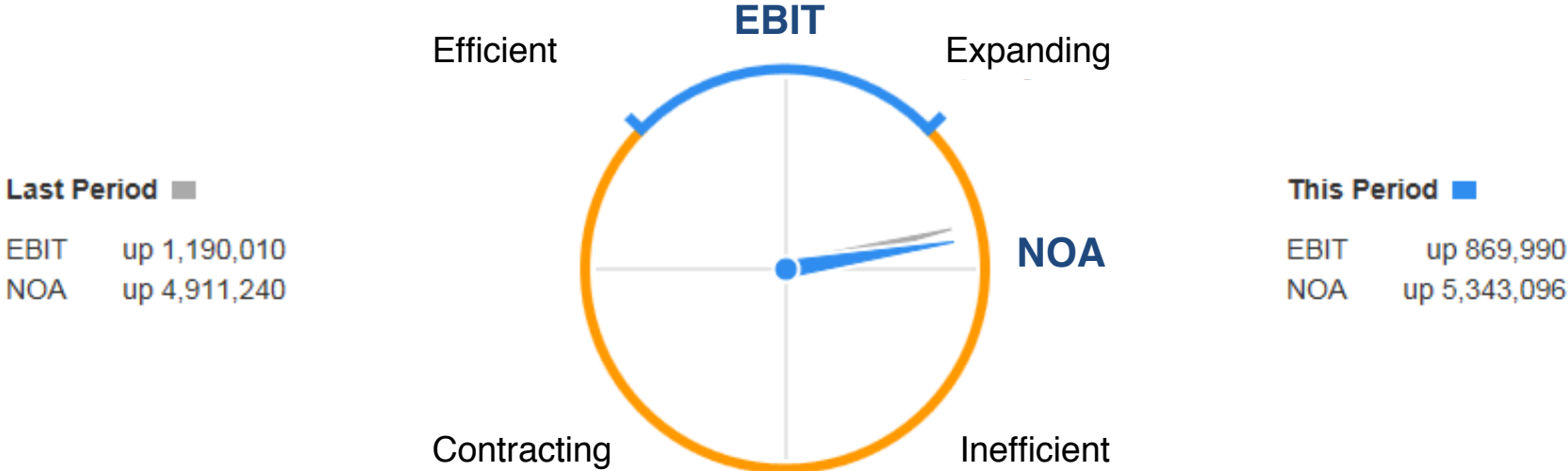
KEY POINTS

- Clear understanding of what the business is doing
- Which quadrant is the business in now, where is it heading and why?
- What are the opportunities for the business?
- What will the outcomes be for the business
- There are options and the answer is 'it depends'
- This provides a powerful partnership tool



Optimizing Growth

Your Growth Strategy





Improving Returns by understanding your Customers

Most companies operate under the 80/20 rule.





Improving Returns by understanding your Customers

They want
a relationship

They don't want
a relationship

We
want a
relationship

1

2

We don't want
a relationship

3

4



What do we do with 3 & 4s?

They want
a relationship

They don't want
a relationship

We
want a
relationship

1

2

We don't want
a relationship

3?

4?



What do we do with 3 & 4s?

They want
a relationship

They don't want
a relationship

We
want a
relationship

1

2

We don't want
a relationship

Increase Price
Enforce strict terms



What do we do with 1 & 2s?

The goal is to identify your blind spots with your 1 and 2 clients and lock them into your business.

- Ask these key clients for a wish list (i.e. what do we need to do to at least be equal with your best supplier?)
- Provide these clients with your wish list (i.e. what we want from them)
- Document a supply chain agreement.



1



2



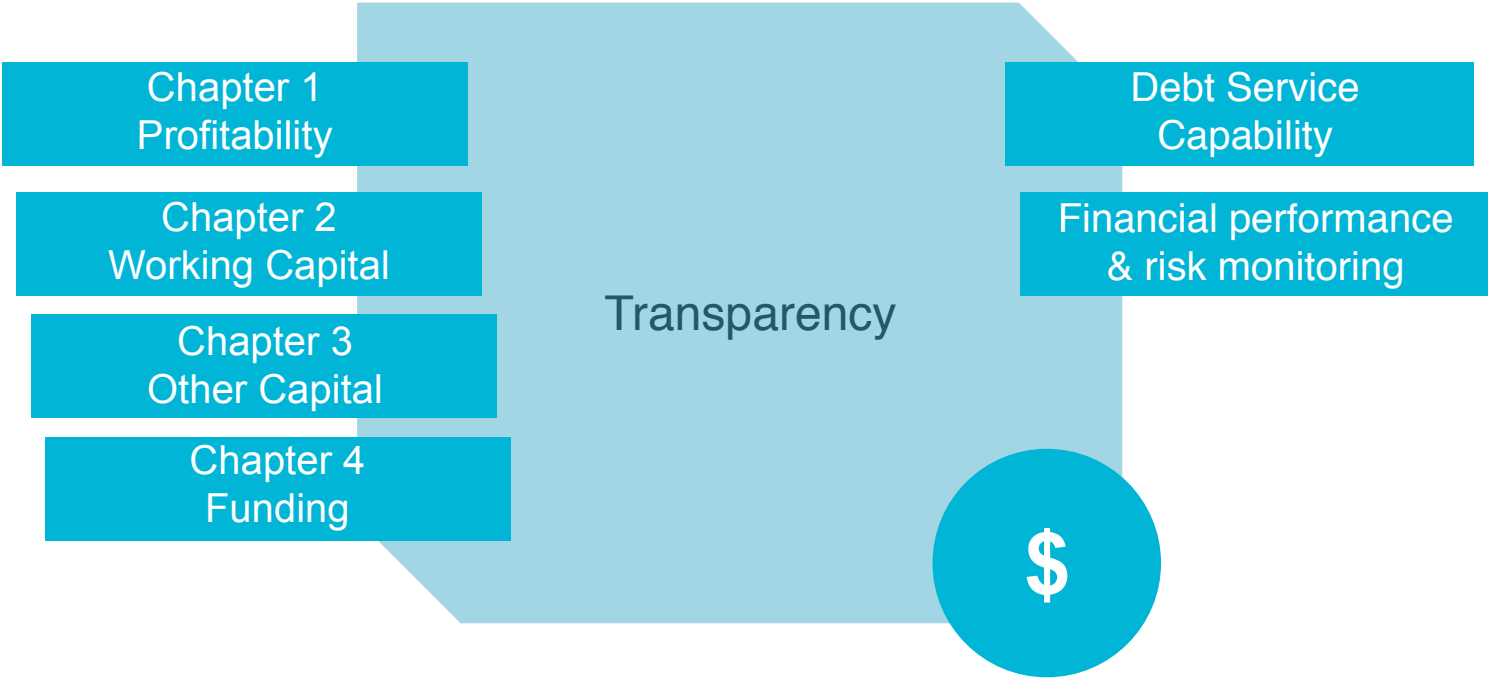
The role of Finance

Finance's role is to measure your company from a **business** and **banking** perspective.

The Financial Health Check

Business Perspective

Bank Perspective





Important Concepts to be used in the 4 Chapters

Chapter 1 - Profitability

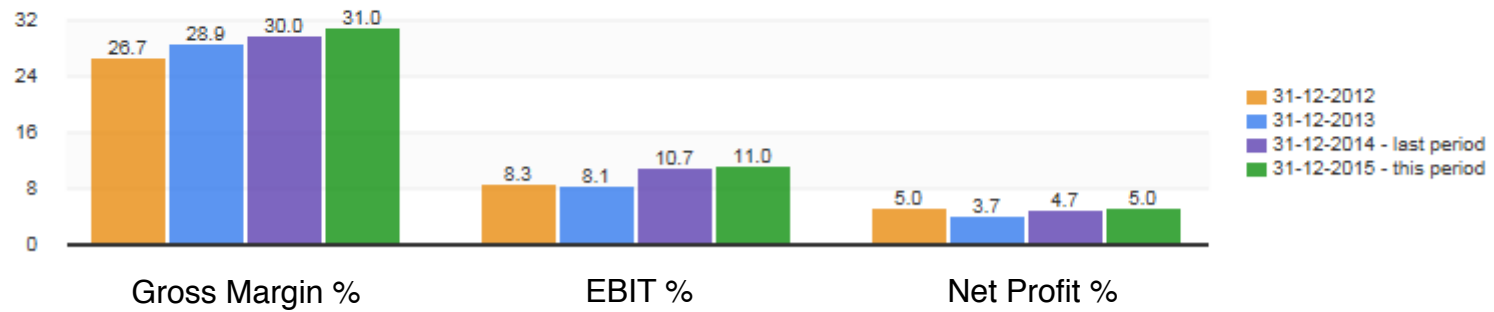
Chapter 2 - Working Capital

Chapter 3 - Other Capital

Chapter 4 - Funding

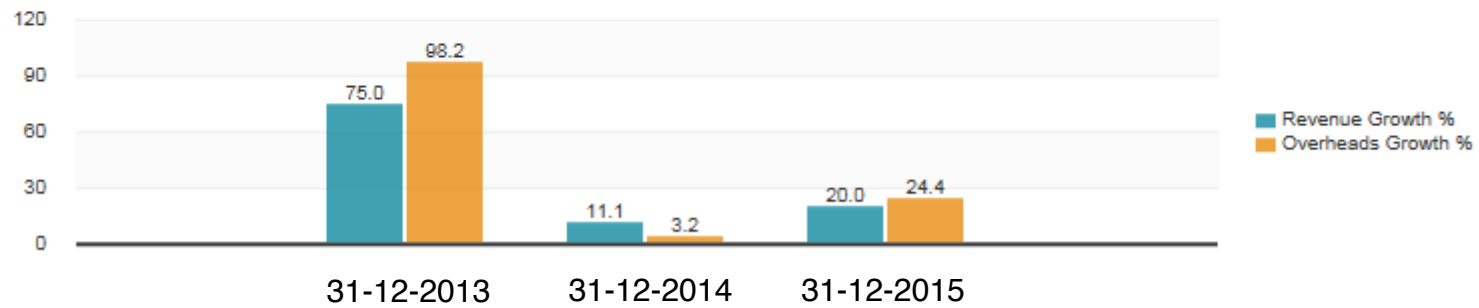
Chapter 1 - Profitability

Profitability Trends



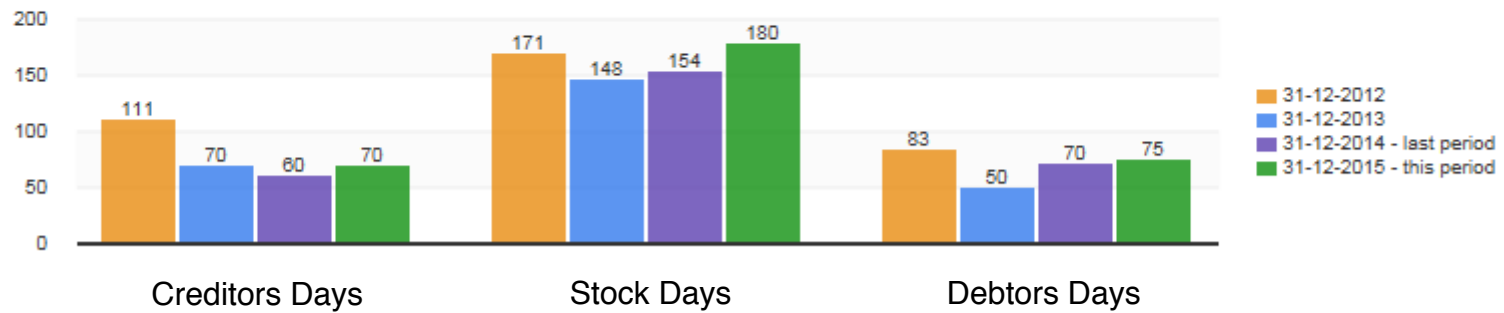
Chapter 1 - Profitability

Revenue Growth vs Overheads Growth



Chapter 2 - Working Capital

Working Capital Days



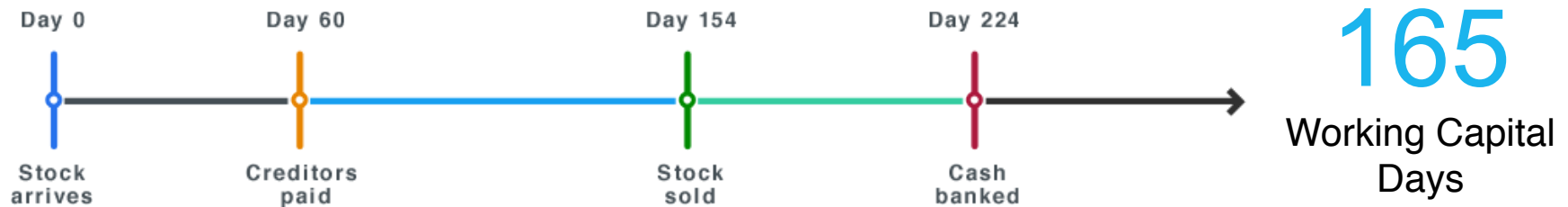
Chapter 2 - Working Capital

Working Capital Timeline at 31-12-2015

This Period

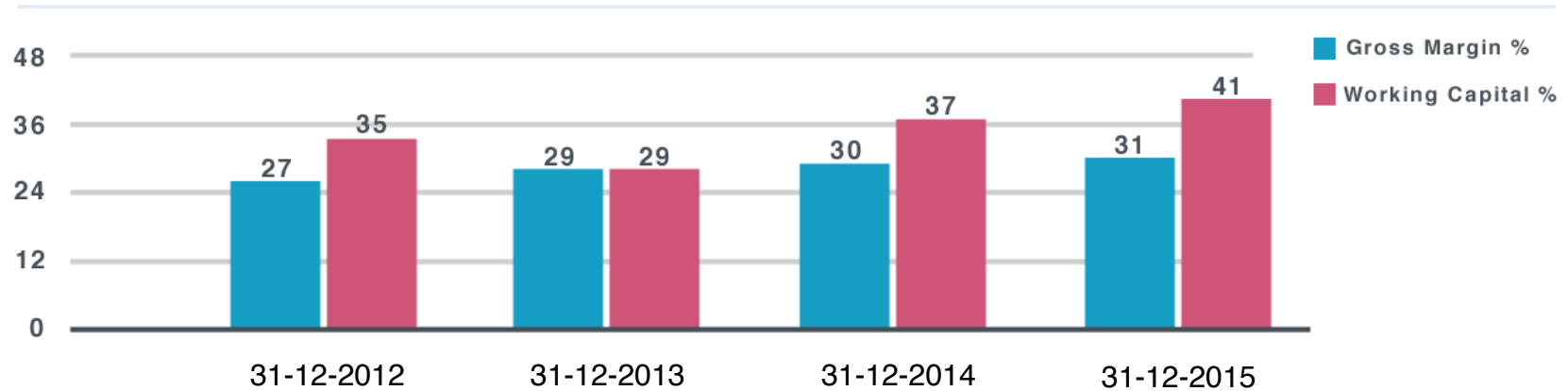


Last Period

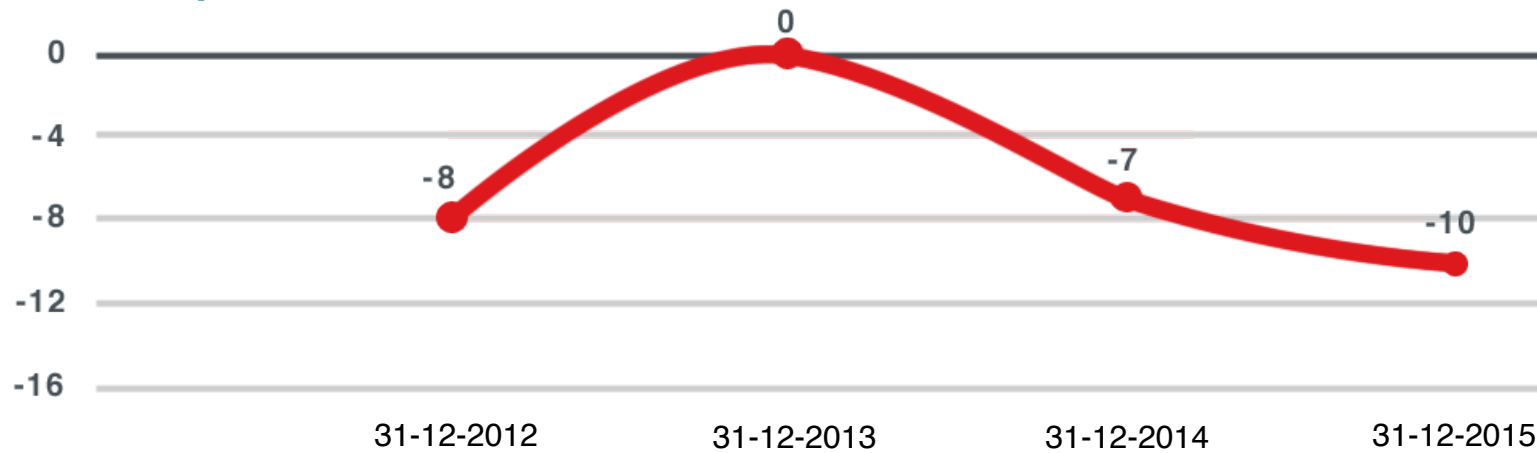


Chapter 2 - Working Capital

Gross Margin vs Working Capital

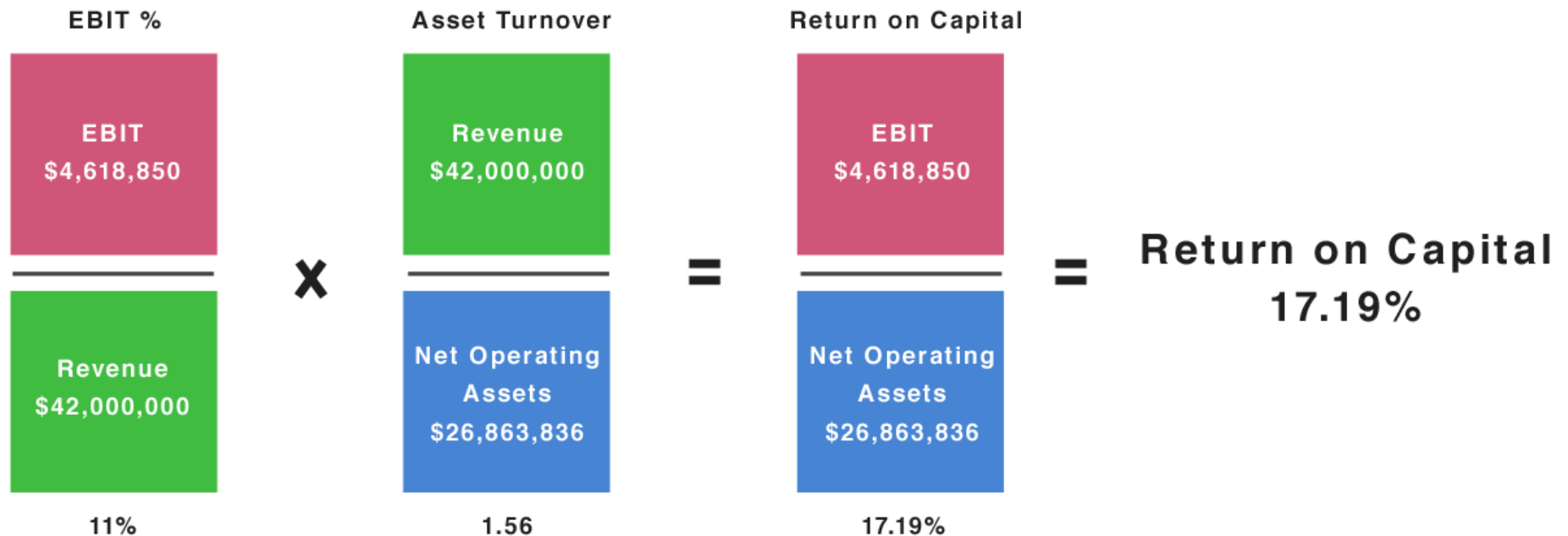


Your Gap



Chapter 3 - Other Capital

Return on capital %





Chapter 4 - Funding

Your Big 3 Cash Flow Measures

- Marginal Cash Flow
- Operating Cash Flow
- Net Cash Flow



Marginal Cash Flow

The additional cash that will be generated or used up if we sell \$1 more of our product or services.

*Note:
this should be a year to date
measure*



Marginal Cash Flow for the next \$1 of sales

Gross margin	13,020/42,000
<i>Less</i>	
Debtors	8,630
Inventory/WIP	14,291
Creditors	(5,557)
<hr/>	
Working Capital	17,364/42,000



Marginal Cash Flow for the next \$1 of sales

Gross margin	31.00 cents
<i>Less</i>	
Debtors	20.55
Inventory/WIP	34.03
Creditors	(13.23)
Working Capital	41.34 cents
<hr/>	
Cash outflow	(10.34) cents
<hr/>	

Divisional Review

Divisional comparisons	GM%	AR Days	WIP Days	WC%	GM%-WC%	Rank
Brisbane Design	47	163	91	67	-20	17
Brisbane Planning	45	106	38	37	8	9
Brisbane Property	25	67	42	26	-1	13
Consumer Research	48	90	12	25	23	3
International Property	58	132	42	45	13	7
Melbourne Design	31	30	23	11	20	5
Melbourne Economics	48	60	15	18	30	1
Melbourne Planning	50	76	30	27	23	3
Perth Design	30	56	44	24	6	11
Perth Planning	29	59	22	18	11	8
Sydney Design	46	66	45	28	18	6
Sydney Heritage	12	37	58	21	-9	16
Sydney Planning	50	82	24	26	24	2
Sydney Property	29	104	21	31	-2	14
Sydney Social Policy	37	67	80	37	0	12
Telco	16	78	20	23	-7	15
Valuation	46	78	72	39	7	10
Total	38	79	40	30	8	



Operating Cash Flow

Profit vs Cash Flow

Profit		Cash Flow		Variance
Revenue	42,000,000	Cash from Customers	40,082,193	-1,917,807
COGS/DC	28,980,000	Cash to Suppliers	31,405,289	-2,425,289
Gross Margin	13,020,000	Gross Cash Profit	8,676,904	-4,343,096
Overheads excl Depreciation	8,400,000	Overheads excl Depreciation	8,400,000	-
EBITDA	4,620,000	Operating Cash Flow	276,904	-4,343,096

Note: this should be a monthly measure



Net Cash Flow

Opening net debt

Cash	0
Short term debt	5,019,740
Long term debt	9,000,000

14,019,740

Closing net debt

Cash	0
Short term debt	7,279,813
Long term debt	10,000,000

17,279,813

Net cash flow **-3,260,073**



The quality of your cash flow:

Impact on cash flow			
	Strengths	Weakness	Next Period
Profitability			
Working Capital			
Other Capital			
Funding			

For each measure let's look at...

Profitability	Ideal Profile	G	A	B
Sales	100			
GM %	30	>30	28-30	<28
OH %	20	<20	20-22	<22
EBIT %	10	>10	8-10	<8
Working Capital				
Debtors Days	60	<60	60-70	>70
Inv/WIP Days	90	<90	90-100	>100
Creditors Days	60	45-60	60-70	<45>70
Working Capital %	22	<22	22-25	>25

William's Numbers:

Profitability	Ideal Profile	G	A	B
Sales	100			
GM %	30	31		
OH %	20		20	
EBIT %	10	11		
Working Capital				
Debtors Days	60			75
Inv/WIP Days	90			180
Creditors Days	60		(70)	
Working Capital %	22			41



The Power of One - Sensitivity

Your 7 levers to improve Profit, Cash Flow and Business Value:

- Price %
- Volume %
- COGS %
- Overheads %
- Debtors
- Inventory/WIP
- Creditors

The Power of One

Your Power of One		Net Cash Flow \$	EBIT \$
Your Current Position		-3,260,073	4,618,850
Your Power of One	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> <input type="button" value="Reset"/>	Impact on Cash Flow \$	Impact on EBIT \$
Price Increase %	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> %	333,699	420,000
Volume Increase %	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> %	-43,438	130,200
COGS Reduction %	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> %	377,137	289,800
Overheads Reduction %	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> %	84,012	84,012
Reduction in Debtors Days	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> days	115,068	
Reduction in Stock Days	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> days	79,397	
Increase in Creditors Days	<input type="button" value="-"/> <input type="text" value="1.0"/> <input type="button" value="+"/> days	79,397	
Your Power of One Impact		1,025,272	924,012
Your Power of One		Net Cash Flow \$	EBIT \$
Your Adjusted Position		-2,234,801	5,542,862

The Power of One – William's strategy



Your Power of One		Net Cash Flow \$	EBIT \$
Your Current Position		-3,260,073	4,618,850
Your Power of One	- 1.0 + <input type="button" value="Reset"/>	Impact on Cash Flow \$	Impact on EBIT \$
Price Increase %	- 1.0 + %	333,699	420,000
Volume Increase %	- 0.0 + %	0	0
COGS Reduction %	- 0.0 + %	0	0
Overheads Reduction %	- 2.0 + %	168,023	168,023
Reduction in Debtors Days	- 5.0 + days	575,342	
Reduction in Stock Days	- 15.0 + days	1,190,959	
Increase in Creditors Days	- 0.0 + days	0	
Your Power of One Impact		2,268,023	588,023
Your Power of One		Net Cash Flow \$	EBIT \$
Your Adjusted Position		-992,050	5,206,873

Your Business Value Indicator

Your Business Value Indicator

Weighted Average EBITDA	\$	5,118,067
Your Expected Business Value	\$	15000000

Your Current Business Value Indicator

EBITDA Multiple	 	4
EBITDA Valuation of Your Business		20,472,268
Less Total Debt		17,279,813
Your Equity Valuation		3,192,455
Your Actual Equity		9,584,023

Your Business Value Indicator – Power of One Value Uplift

Price +1%
Overheads down 2%
Debtors reduced by 5 days
Inventory reduced by 15 days

Your Value Improvement

+ Your Power of One Value Uplift

EBITDA Multiple	← →	4
Your Power of One Impact		4,118,393

Your Enhanced Value Indicator

Your Equity Valuation	3,192,455
Your Power of One Impact	4,118,393
Your Enhanced Equity Indicator	7,310,848

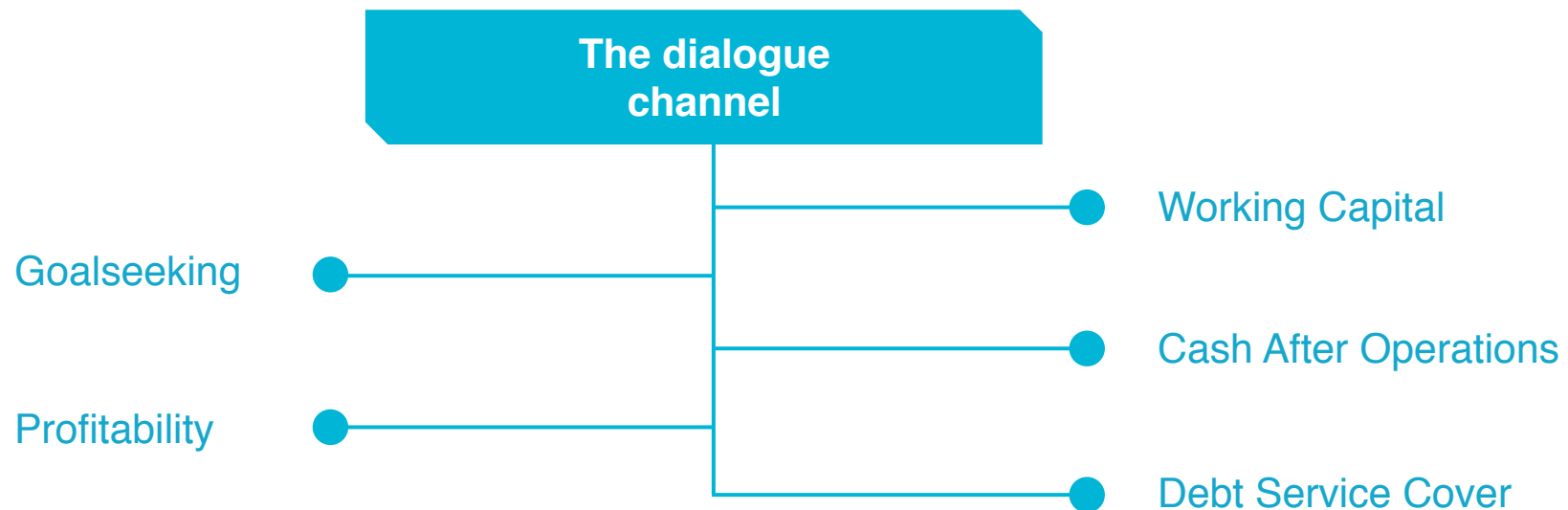
Your Business Value Indicator – Power of One Value Uplift

Your Value Improvement	
- Your Power of One Value Uplift	
EBITDA Multiple	4
Price Increase (1%)	1,680,00
Volume Increase (0%)	0
COGS Reduction (0%)	0
Overheads Reduction (2%)	672,092
Profit Impact on Valuation	2,352,092
Reduction in Debtors Days (5d)	575,342
Reduction in Stock Days (15d)	1,190,959
Increase in Creditors Days (0d)	0
Cash Impact on Valuation	1,766,301
Your Power of One Impact	4,118,393

Core Credit Principle

Only lend what the Customer has the capacity and ability to repay

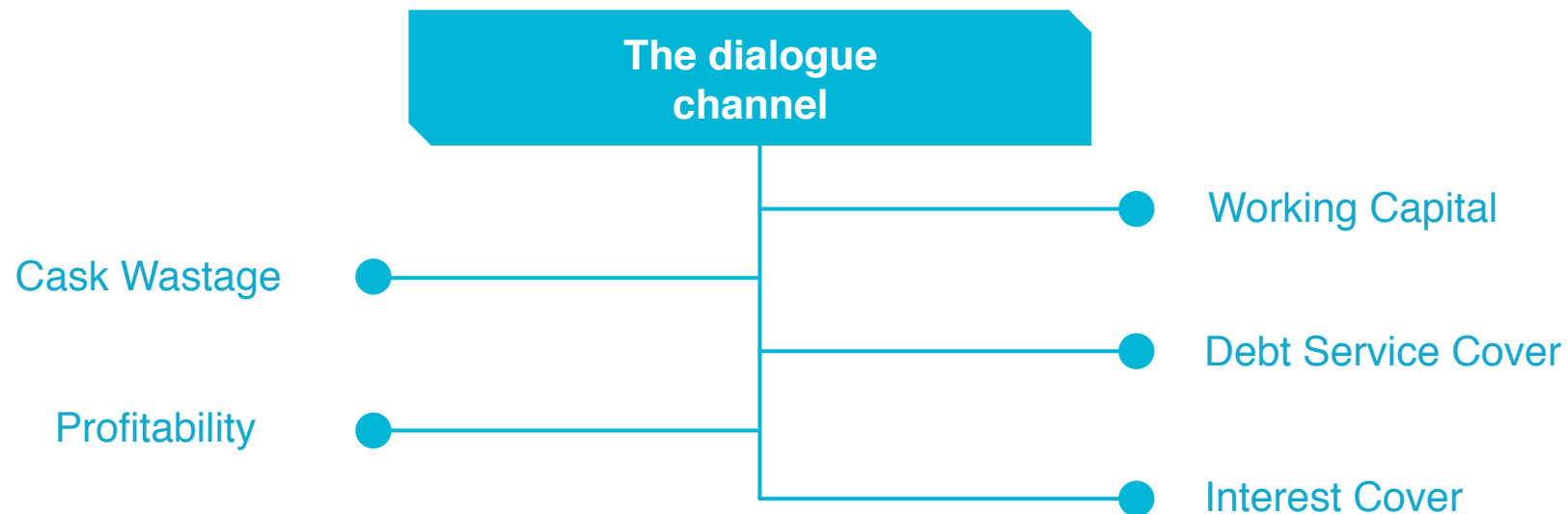
- Today's debt is repaid from tomorrow's cash flow – assumptions? (Capacity to service)
- Cash Flow Quality
- The need for debt and how it arises
- Fast growth symptoms and consequences



Core Credit Principle:

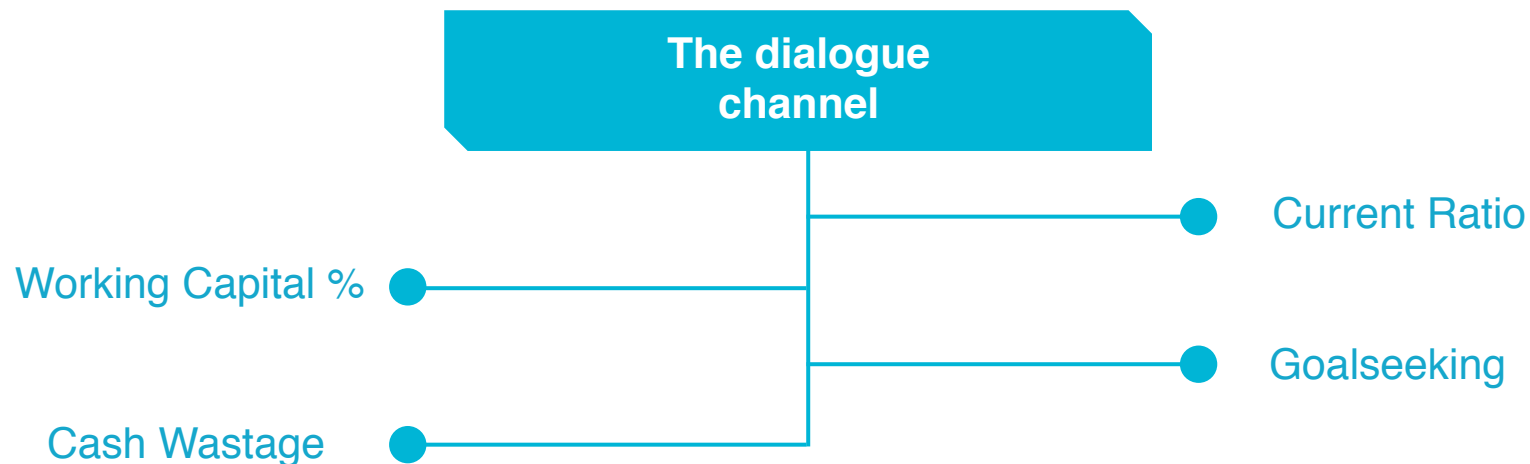
Be proactive in identifying, managing & communicating risk

- Early warning indicators of credit deterioration
- Positive recognition of customer's strong or improved performance
 - Profitability
 - Working Capital Management
 - Non Current Assets
 - Cash Flow & Funding
- Covenants and feedback procedures
- Stress testing assumptions



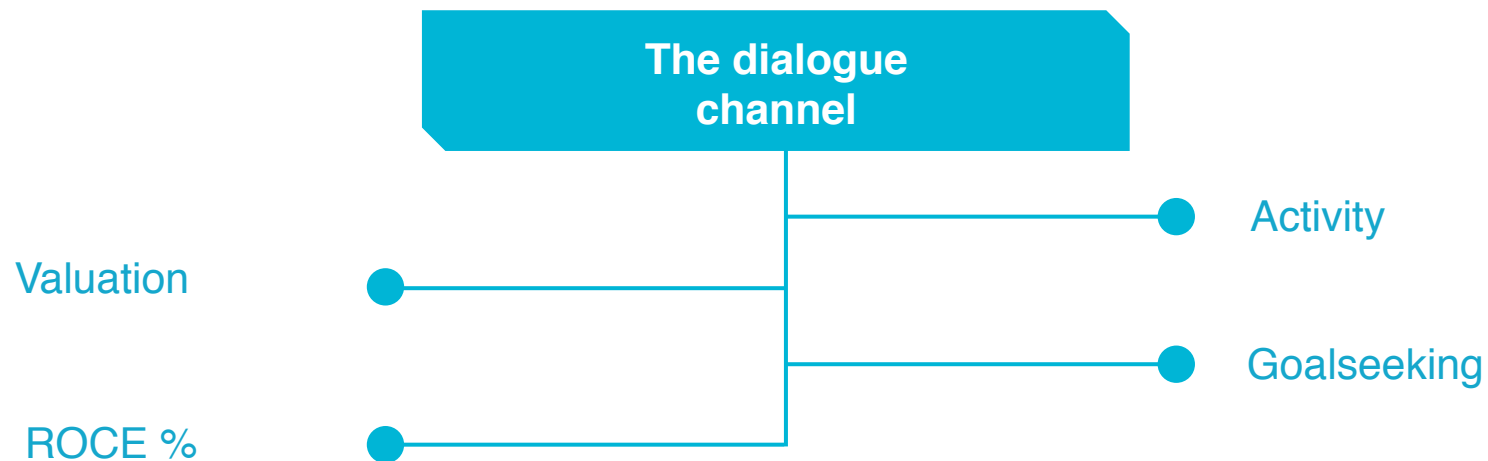
Short Term Liquidity

- Working Capital Management
- The impacts of fast growth
- The drivers of operating working capital investment



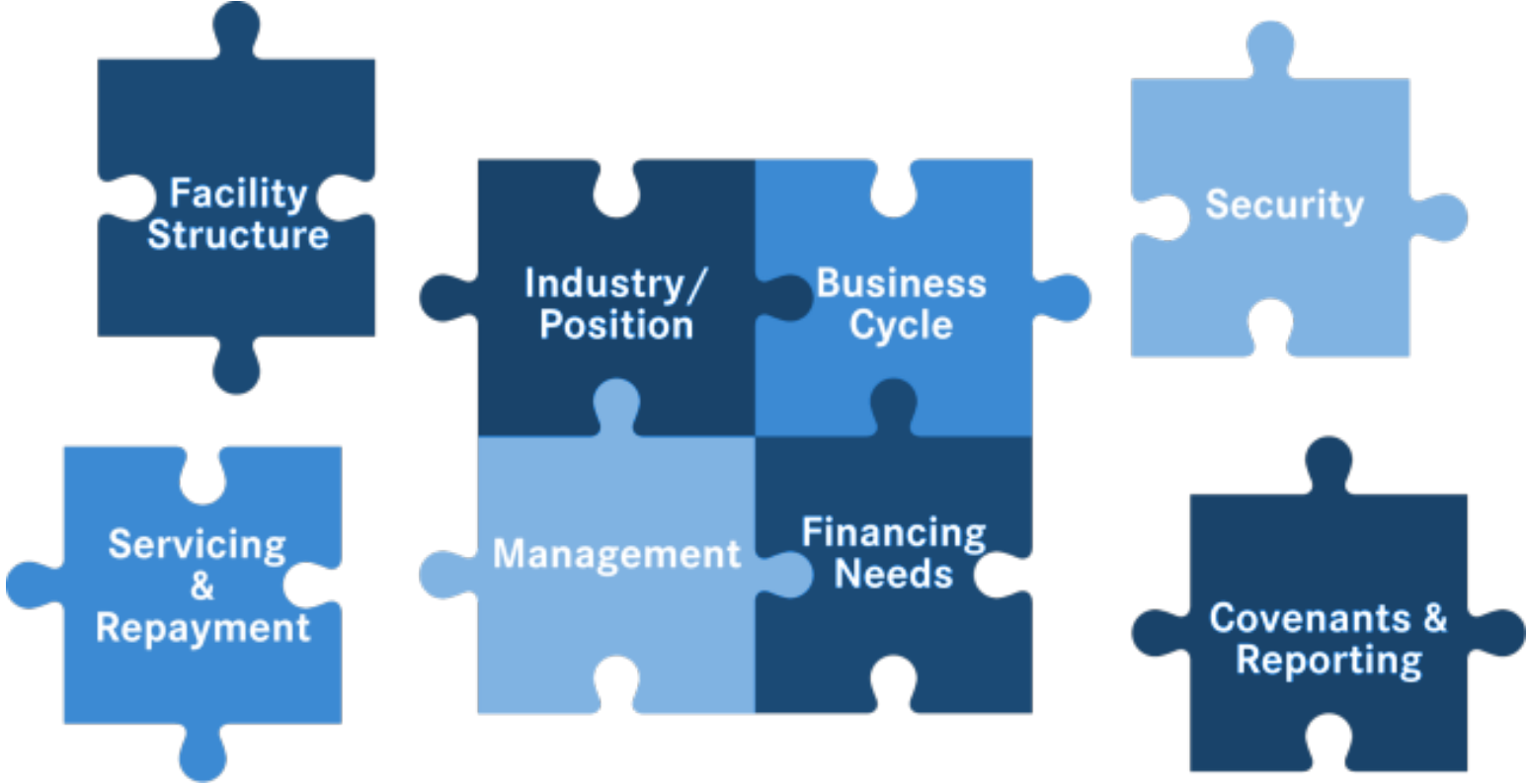
Long Term Solvency

- The Balance Sheet structure
- Valuing the Net Assets





Understanding the customer





The top 5 frustrations Business has with Banks

- They don't understand my business
- They are inflexible
- They are never there when I need them
- My manager keeps changing
- They take forever to make a decision



The top 5 frustrations Banks have with Business

- They don't treat us like a partner in the business
- They don't forecast or budget accurately.
- They keep changing directions without letting us know
- You never know when things are going bad – it's a surprise and that is bad for my career
- Just when we get on they shop us with another bank



William's Plumbing Bank Scenario

- William has requested 5 increases in facilities in 3 years.
- William has just had a switch of manager who has immediately flagged concern, and the “Hospital Division” of the bank has taken note
- Hospital Division wants to appoint an Investigative Accountant to review the numbers at a cost of \$60k to Williams



3 things every bank decision should consider

- **Management** – best assessed by financial performance and forecast accuracy
- **Debt Service Ability** – Once you are comfortable that the numbers presented are accurate, does the business meet servicing ratios
- **Security** – If the business defaults on its obligations is the lender exposed to possible loss after it exercises its rights under the security agreements



Our Recommendations for William's Plumbing

1. Bank Communication – Build Advocacy and Remove the Investigative Accountant Need
2. Financial Management – Reporting
3. Restructure – Implement Working Capital Change
4. Bank Restructure – Change the facilities



How dependant are you on your bank?

If your bank decided to cease your relationship would your business survive?

- Would you be solvent?
- Could you trade/purchase goods?
- Do your sales depend on your Merchant terminals?
- Do you need internet banking?
- Do you pay your wages through the bank?

What is your current strategy to mitigate this risk?



Who woke up this morning thinking of your business?

How important are you to your key stakeholders?

- Major Customers?
- Major Suppliers?
- Your Employees?
- Shareholders?
- Your Bank?

Old bank relationship model vs New

Old Model

Your Bank Manager managed you



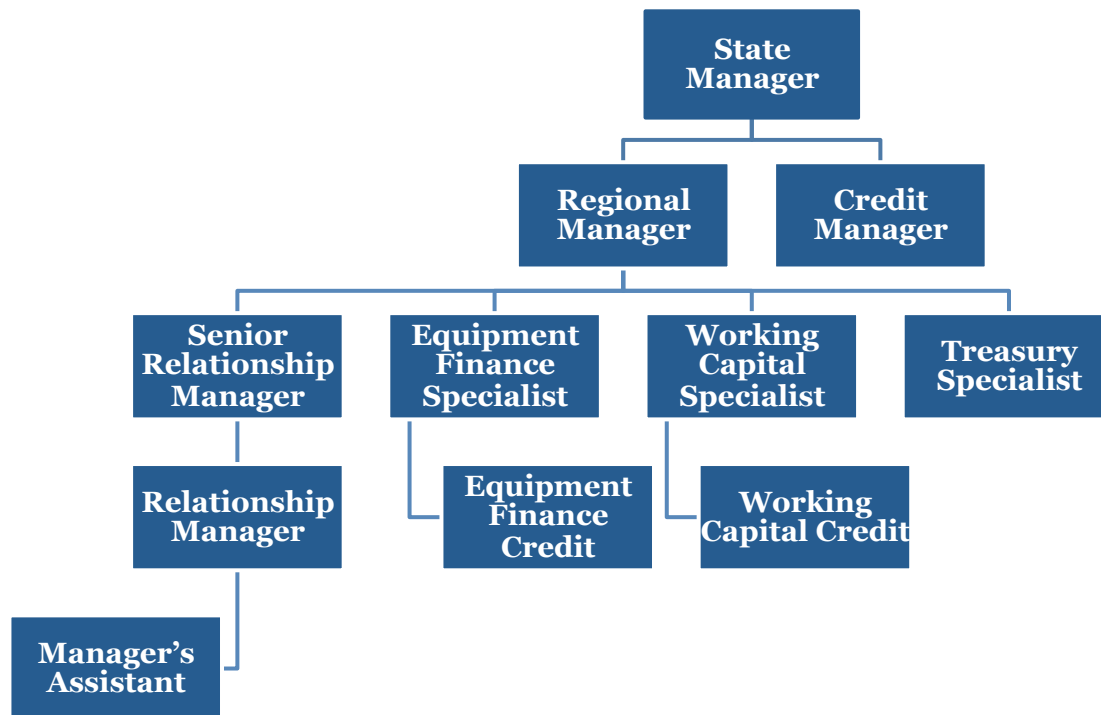
New Model

You need to manage your bank!



Active Networking

To secure a sustainable long term bank relationship you need to have a minimum of 5 advocates of your business working in the bank.



How many advocates do you have currently?



How do you build Advocacy?

- Partner – Let bankers feel like their contribution to the business matters
- Give them a voice – Let them express opinions and allow them to feel like you consider their input valuable
- Reciprocation – Your bank will feel more inclined to support your business if you support theirs. Refer friends to them, buy from them, allow them opportunity to promote their services within your networks
- Provide social recognition – Invite them to your events, thank them for their support in public and on social media. Make them feel special



Messages to reinforce

- Give a clear understanding of the exciting future of the business
- Consistently predict the future with reasonable accuracy
- Governance! – your risk management, systems and controls are meticulously planned and executed
- Financial competence – your numbers are accurate and trustworthy
- Cash flow positive and profitable – your strategy is working

RULE 1: NO SURPRISES

- Are you a safe pair of hands for your bank's money?

Business Planning

You must use a 3 way Budget – ie P & L, Balance Sheet and Cash Flow

Your Budget needs to make sense!

- Does it balance?
- Does align with your plan?
- Does it show the bank what you need of them?
- Do the basic ratios relate with the past?

	Last Year	This Year	Comments
Revenue	\$17,564,890	\$19,145,730	2 new clients
Revenue Growth	8%	9%	
Gross Profit %	52%	53%	Pay 30days earlier
Operating Exp %	45%	43%	Cheaper Rent
EBIT %	7%	10%	
Acc Rec (Days)	43 Days	43 Days	No change
Inventory (Days)	120 Days	100 Days	Stock elimination
Acc Pay (Days)	30 Days	32 Days	
Net Cash Movt	+\$900,000	+\$1,200,000	
RONA	18%	24%	Target 25%
ST Debt Balance	\$2,000,000	\$1,500,000	
LT Debt Balance	\$6,000,000	\$5,500,000	
Interest Cover	3.4x	6.1x	Strong Improve



Next Steps

1. Ensure the senior staff understand all the concepts in “Cash Flow Story” – The Four Chapters, The Big Three Cash Flow numbers - Please review the training video at www.cashflowstory.com/resources.
2. Create a monthly or quarterly financial scorecard using the four chapters. Set monthly or quarterly targets. Ensure these targets are communicated to all key Staff
3. Have a monthly/quarterly management meeting. (The template provided can be the basis of the meeting)
4. Set a “theme” in the business on a quarterly basis so that your company can celebrate success 4 times a year. Ensure that the critical numbers are communicated and understood
5. On a quarterly basis calculate the Power of One of your company and discuss at the management meeting. (Cash Flow Story can calculate the number)
6. The Power of One will help drive change management in the business
7. Ensure that your company has a 12 months rolling budget. (Cash Flow Story can assist in the high level budgeting process)
8. Ensure that you understand the way the bank is viewing your business

Stay in Touch!



Thank you!

Click on the [Video Summary](#) or go to www.cashflowstory.com/resources to watch a summary of this talk

To receive a copy of this presentation and exclusive access to a copy of our Monthly Reporting Template

<https://mycashflowstory.com/exclusive>



Questions?