



FutureRoute
the thinking solutions company

Forum of Private Business
and
Future Route

Research Report
Finance and Credit
Management

January 2010

Introduction

The Forum of Private Business (FPB) is a proactive, not-for-profit organisation, providing comprehensive support, protection and reassurance to small businesses. Future Route delivers insight to business strategists in data intensive markets. The company has recently developed a product called Validis that extracts data from management accounts to help business owners manage and interrogate their financial information.

Summary of findings

These are the main summary of the findings:

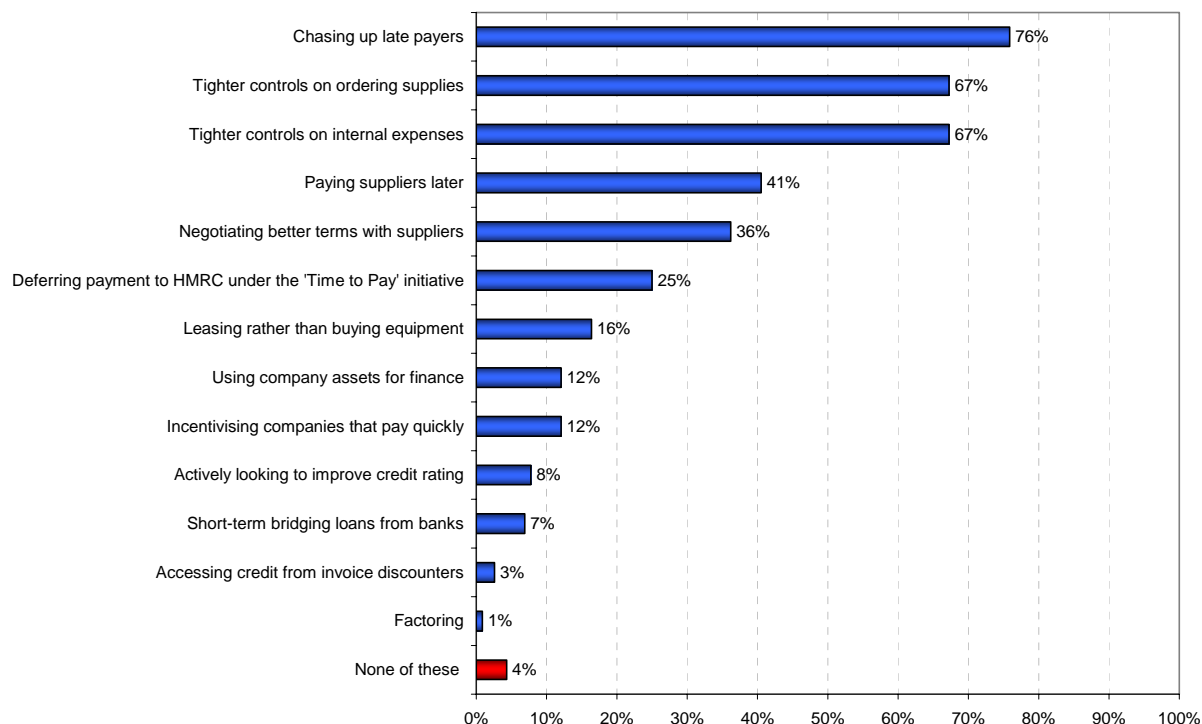
- Cash flow in 2009 has been a big problem for businesses of all sizes. As a result, 96% of businesses have looked to improve their cash flow by a variety of methods such as chasing up late payers or introducing tighter controls on internal spending.
- In general, businesses have been successful in their ways of improving cash flow, particularly in delaying payment of tax by taking advantage of HMRC's scheme. The exception is improving their credit rating.
- Currently, audited accounts, credit checks and management accounts all have their limitations, particularly in terms of the timeliness – or rather untimeliness – of the data. Nevertheless management accounts are the most common way in which businesses are minimising financial risks.
- With a greater onus on businesses to show that they deserve credit despite the limited financial resources, businesses are prepared to grant access to their management accounts to banks.
- There is a reluctance to provide information to other third parties, particularly utilities companies, as there is a concern as to what the information would be used for. Just 9% of business owners would be prepared to offer full disclosure of management accounts to their supply chain.
- Around two thirds of business owners use management accounts, with the majority being done in-house.
- The advantages of management accounts are broadly accepted by small business owners. The majority of respondents cited the key advantages as providing financial information to enable owners to effectively manage their businesses.
- The disadvantages of management accounts focus on how they could be used by their supply chain to renegotiate terms to the detriment of their business. This is a particular concern at the moment, with a large number of businesses having relatively weak financial figures.

Ways of managing cash flow

96% of respondents have looked to improve or manage more closely their cash flow over the last 12 months as a direct response to the recession. Tighter internal controls on spending (67%) and chasing up late payers (76%) were the most commonly used methods to manage cash flow.

41% also paid their suppliers later and 25% deferred payment through the HMRC 'Time to Pay' scheme – all of which are temporary solutions and could lead to issues in the future. Negotiating terms with suppliers was utilised by almost as many businesses as those that paid suppliers late. In some cases, this appears to have been a time/workload issue, as those with limited resources in their finance departments were more likely to pay later, whilst those with larger departments were more likely to negotiate. A significant proportion did both.

Figure 1: Ways companies have managed or improved cash flow over the last 18 months



Apart from accessing credit from invoice discounters, which was used by a relatively low number of respondents, leasing and the Time to Pay initiative were the most successful of the steps that businesses introduced, with a score of 7 out of 10. Tightening internal controls on spending was also fairly successful, with tightening of controls on expenses marginally better than on ordering supplies.

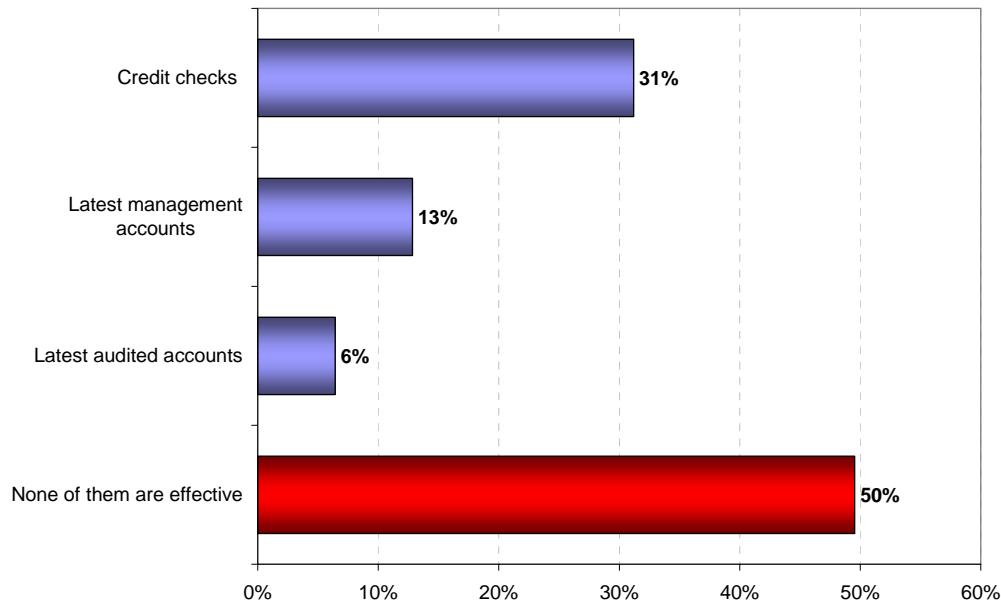
Figure 2: Success in managing or improving cash flow over the last 18 months

	Proportion cutting costs	Very successful	Fairly successful	Unsuccessful	Success rating
Negotiating better terms with suppliers	36%	19%	74%	7%	5.6
Paying suppliers later	41%	19%	79%	2%	5.9
Chasing up late payers	76%	29%	59%	13%	5.8
Incentivising companies that pay quickly	12%	15%	77%	8%	5.4
Using company assets for finance	12%	43%	43%	14%	6.4
Short-term bridging loans from banks	7%	29%	57%	14%	5.7
Accessing credit from invoice discounters	3%	67%	33%	0%	8.3
Leasing rather than buying equipment	16%	50%	50%	0%	7.5
Factoring	<1%	0%	100%	0%	5.0
Deferring payment to HMRC under the Time to Pay initiative	25%	62%	31%	7%	7.8
Actively looking to improve credit rating	8%	11%	67%	22%	4.4
Tighter controls on ordering supplies	67%	38%	56%	5%	6.7
Tighter controls on internal expenses	67%	41%	54%	5%	6.8

Those looking to improve their credit rating cited this as the least successful of the measures that businesses tried to improve cash flow. This is mainly due to factors outside the control of the businesses, namely the risk aversion of credit agencies.

Nevertheless, respondents felt that credit checks were the most effective way of checking on suppliers and customers, although there were issues with all types of information used to monitor the supply chain.

Figure 3: Most effective way of monitoring your supply chain



Credit checks were the most frequently mentioned as they provide useful trends and are perceived to give the most accurate view of the company's financial stability as it takes information from a variety of sources. However, even those respondents who did mention this indicated it was only useful as part of a wider monitoring service which included contacting other suppliers or getting data from Companies House.

Those that mentioned the latest management accounts indicated that these were timely and provided sufficient information on the company's finances on a day-to-day basis. However, respondents who mentioned this pointed out that, in order to access such information, you have to have a good working relationship with each link in your supply chain.

Audited accounts were seen as reliable and evidence-based, and the basis for credit checks anyway.

Each measure had its own problems, though; many felt that management accounts were not cost effective, credit checks and audited accounts were not updated quickly enough and companies can still hide major problems from their supply chain. Respondents were also worried about losing customers and even suppliers if they asked for their latest management accounts.

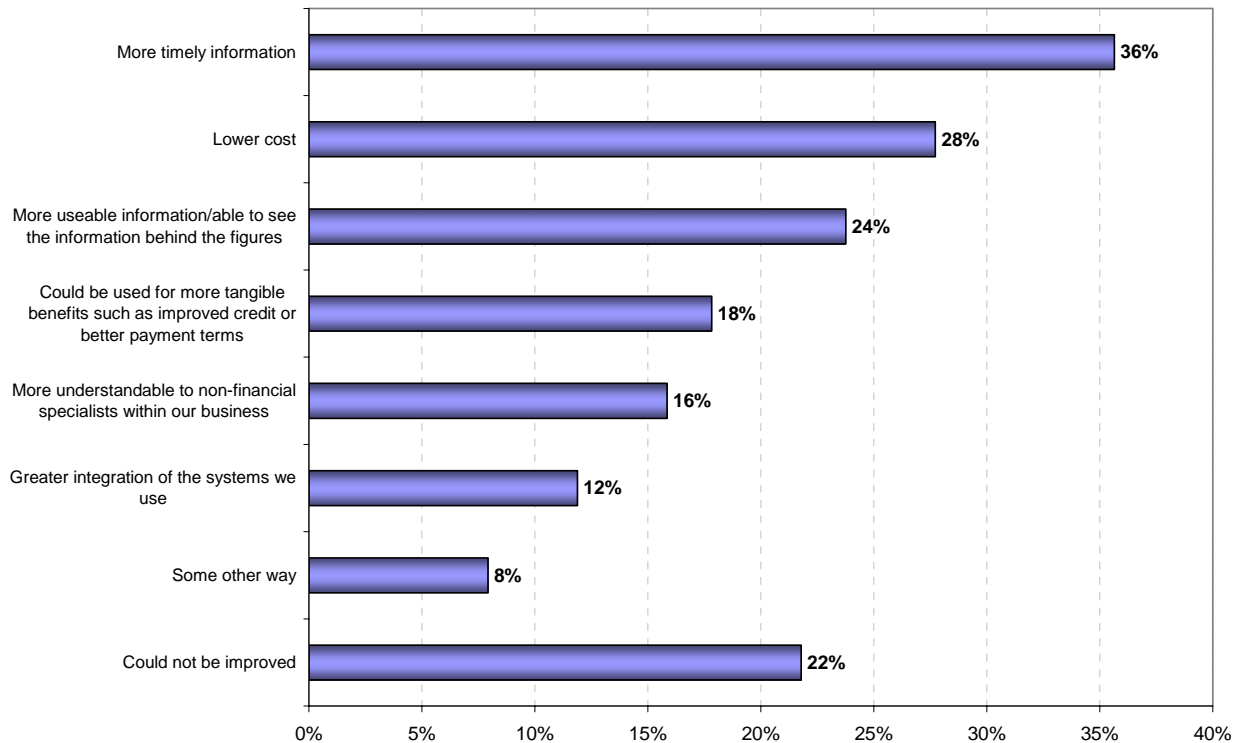
Businesses without a finance department or where the owner looks after the finance were more likely to use informal methods of checking on suppliers and customers. Credit checks on customers and the production of regular management accounts were the most regular for businesses generally with incidents of this increasing in direct correlation with the number of people in the finance department.

Figure 4: Ways in which owners have minimised financial risk to their businesses

	Total	Number of people in finance department		
		None	One	Two or more
Credit checks on key suppliers through a credit reference agency	17%	13%	19%	22%
Credit checks on key customers through a credit reference agency	41%	33%	51%	41%
We buy in the latest accounts from Companies House	9%	8%	3%	19%
We ask key suppliers for their latest management accounts	2%	2%	3%	0%
We ask key customers for their latest management accounts	6%	4%	5%	7%
We ask prospects for their latest management accounts	3%	2%	3%	4%
We have a credit insurance policy	6%	6%	3%	11%
We have regular meetings with our auditor/external accountant	18%	13%	19%	22%
We produce regular management accounts internally	48%	33%	54%	70%
We provide annual audited accounts to Companies House	32%	15%	38%	56%
Other steps used	17%	17%	19%	15%
None of these steps are taken	22%	31%	14%	15%

78% of respondents would like to see the information provided to their businesses improve in some way in the future to minimise the financial risk that they expose themselves to through suppliers and customers. The main way to minimise financial risk to the company is through the provision of more timely information, allowing risks to be more accurately assessed. Other important ways to improve the quality of the information is to lower the cost, making a wider range of options more accessible. Ability to interrogate the data is also important in terms of letting the owner understand and use the information behind the figures to cut costs and improve efficiency.

Figure 5: Ways to improve the quality of information provided to minimise financial risk



As the credit market has tightened, banks have increasingly asked for management accounts as part of allowing companies access to finance. For this reason a large number of businesses have generally accepted this as a necessary evil, otherwise they tend to be happy only with providing internally to directors and senior managers or, where appropriate, non-executive directors.

Figure 6: Who companies would be prepared to provide management accounts to

	Already do	Definitely	Reluctantly	Never
Directors and senior managers	72%	15%	11%	2%
Non executive directors	41%	19%	22%	19%
Banks	58%	24%	17%	1%
Invoice discounters or other financiers	18%	20%	35%	27%
Utilities companies	3%	4%	27%	66%
Key suppliers	15%	22%	38%	26%
Key customers	11%	21%	27%	41%
Credit reference agencies	10%	21%	40%	29%
Credit insurers	13%	19%	34%	34%
HMRC	19%	28%	42%	11%

There is strong opposition to passing management accounts to utilities companies and to providing such information to customers. In general, third parties would have to show that the benefits outweighed the potential damages. Many businesses do not trust their energy suppliers, whilst there is greater resistance to providing management accounts to their suppliers than to their customers, as the latter are more likely to want to renegotiate deals to the detriment of the business.

In general, respondents would be very reluctant to supply anything more than the bare minimum to their supply chain or utilities companies. 47% of those that would be prepared to provide management accounts would provide the bare minimum (sales figures), 20% would be prepared to put the information in the context of their cost base and 13% (9% of all businesses) would be prepared to offer full disclosure, providing there is some benefit to the business. 19% did not know. Anecdotal comments would indicate that businesses would be prepared to provide more information to their main suppliers (excluding utility companies) than they would to customers or utilities companies.

Usage of management accounts

68% of responding companies now produce management accounts. The main driver for introducing them was to help manage the business (cited by 85% of respondents), 44% had always done management accounts and 30% had introduced them to cut costs. 17% were required to provide management accounts to access credit. Accountants were also an important driver, with 15% of respondents mentioning that the idea to do management accounts had come from them.

61% of respondents produce their management accounts internally, with a further 25% being produced internally with external validation from an accountant. Just 14% had their management accounts done in their entirety by accountants.

71% have them produced monthly or more frequently, 18% have them produced quarterly, with 11% producing management accounts once or twice a year. However, even when companies look to produce monthly management accounts, the information is not always timely, as 5% of businesses who produce monthly management accounts have to wait four weeks or more for the information.

Surprisingly internal management accounts took slightly longer to produce than those that were provided externally or had external validation. This is likely to be due to a number of businesses having to introduce management accounts relatively recently and having not honed the process yet.

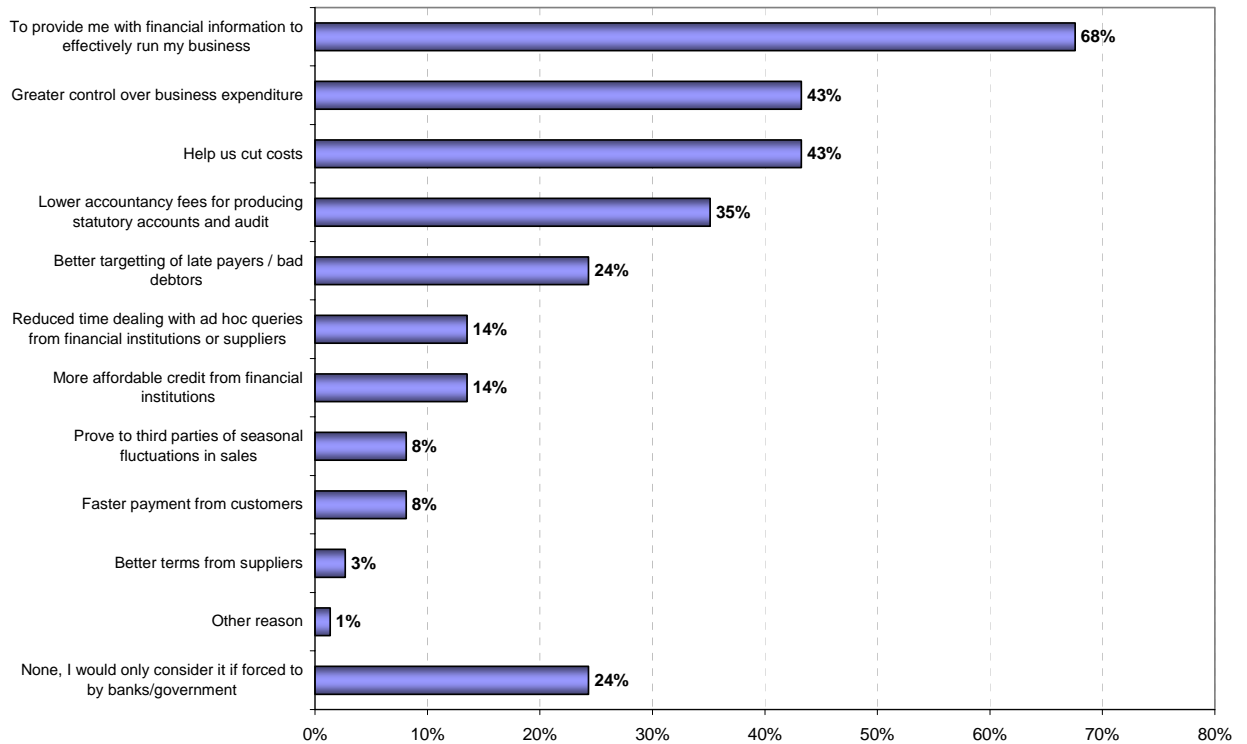
There was a large amount of variation in the costs that businesses paid to accountants for their management accounts, depending on the frequency and level of detail involved. In general, businesses paid an average of £530, with those that had their accounts validated paying less.

Attitudes to management accounts

The majority of respondents felt that the key advantage to producing management accounts was that it gave the owner the information that he needed to run his business. Of those that did not produce management accounts, around 5% did not know how to or felt that there was no benefit to doing management accounts. 87% of respondents felt that they provided financial information to enable them to effectively run their businesses, 53% stated it allowed them to focus on the business issues in hand and 43% felt that it helped them control costs.

The advantages of producing management accounts were not lost on respondents who currently do not use them, as the chart below indicates.

Figure 6: Advantages of producing management accounts



More information

For more information, please contact:

Thomas Parry
Research Projects Manager
Forum of Private Business
Ruskin Chambers
Drury Lane
Knutsford
Cheshire
WA16 6HA

Telephone: 01565 634467
Facsimile: 0870 241 9570
Email: thomas.parry@fpb.org
Website: www.fpb.org

