***Managing working capital: Creditors***

Every business needs supplies of some kind, and every business needs to consider the credit aspect of those supplies.

The problem we all face is that we buy things in to enable us to supply our product or service. Then we bill the customer for the work we’ve done.

So the cash is almost always being paid out before it comes in – leaving us with a cashflow problem.

We can alleviate this problem by getting credit terms from our suppliers. At its simplest this might involve paying for gods with a credit card. I do this with my travel costs, so that I’ve got a fighting chance of having been paid by my client before I have to pay the credit card bill.

Mostly it comes down to negotiating credit terms with suppliers, just as we’ll usually negotiate prices with them.

**Negotiating good terms**

Most of our suppliers will have standard payment terms that they want with their customers. If we don’t negotiate something different, we’re agreeing to their terms. Which could be “You pay in full when you place the order”.

**The compromise with suppliers**

We want suppliers who will:

* make us a priority customer, so we can rely on them when we need them
* give us their lowest possible prices
* give us the longest possible credit terms
* give us the highest quality of goods…
* … and a high quality service

In practice we’re unlikely to find suppliers who will give us all of these! If we pay rock bottom prices, and pay two months late, we’ll struggle to find quality suppliers who want to do business with us.

**Paying on time**

Whatever terms we do negotiate, we need to stick to them. Especially, we need to pay our bills on time. This is especially important if we are a large customer for a small supplier. If we consistently pay late, the resulting cashflow problems could put them out of business. And our reputation will suffer as our company is cited as the cause of failure, and the cause of the resulting redundancies.

We want to have the reputation of a company that is good to do business with. So whatever we negotiate, we deliver.

This means that if part of your job involves approving invoices for payment, you must do this promptly so that the supplier can be paid on time.

**What about discounts for prompt payment?**

These can be worth taking, if we have the cash available to take them.

If we normally pay a supplier in 30 days, and they offer a 2½% discount for payment within 7 days, that’s 2½% for paying 23 days earlier. 23 days is 1/16 of a year (almost), so the 2½% “annualises out” at an equivalent annual rate of 40%, which is considerably less than the overdraft interest we’ll be paying.

Even though 2½% saving on your material costs may not make much difference to those costs, it might make a considerable difference to your profit!