



Chasing Cash Like Pooh chases the Woozle

Now, let's shift the scene to your business.

Sales are skyrocketing, teams are expanding, and ambitious growth plans are on the horizon. It feels like you're hot on the trail of success, just like Pooh with his Woozle. But when you check the bank account, the cash doesn't match the excitement—despite the growth, funds are tight. You're left wondering, "Where did the money go?" It's as if Pooh stopped, scratched his head, and realised he'd been chasing his own tail all along.

THE MISLEADING TRACKS OF RAPID GROWTH**Rapid growth can lay down its own misleading tracks:**

- Excess inventory piling up in warehouses, tying up cash.
- Customers delaying payments, leaving invoices overdue.
- Limited headroom in bank overdraft.

On the surface, it looks like progress—more sales, more activity—but beneath, these "tracks" are sending you in circles. Just like Pooh needed to pause and see the bigger picture, your business needs to step back and focus on the cash flow reality behind the growth.

When you're caught up in the thrill of the chase—new markets, bigger customer bases, higher revenues—it's easy to gloss over the details. But as the saying goes, the devil's in those details. Ignore them, and you might find:

- Warehouses full of unsold stock.
- Overdue invoices stacking up.
- Cash reserves quietly evaporating, even as the top line shines.

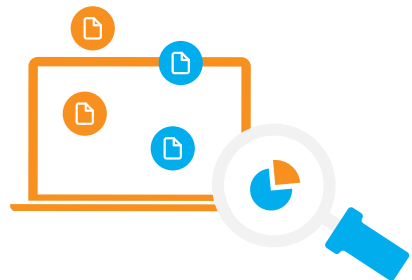
Growth without discipline can lead to some nasty surprises:

- Frustrated bankers and suppliers.
- Liquidity challenges.
- A business valuation that falls short of its potential, disappointing stakeholders.

WHY WCM MATTERS

WCM isn't just for struggling companies or cash-starved startups. It's a strategy for any business looking to:

- Maximize returns on capital employed (RoCE).
- Strengthen liquidity and credit ratings.
- Free up cash for dividends, debt reduction, or reinvestment.



Boost business valuation through **disciplined cash flow management.**

In short, WCM is about turning ambition into sustainable success. It's about ensuring that growth doesn't just look good on paper—it also feels good in the bank account.

What's next?

This guide will walk you through the how-to of WCM, covering:



So, let's step back from the Woozle hunt, take a deep breath, and focus on the tracks that matter. Because in business, as in the Hundred Acre Wood, it's not just about chasing growth—it's about making sure you've got the cash to enjoy the honey when you get there.

What is working capital management?

Working capital management is the act of controlling, handling, directing and monitoring a business's inventory, debtors and creditors.

The operating working capital cycle can be expressed at the aggregated balance sheet level as:

Net working capital (NWC) = current assets – current liabilities.

Alternatively, at the operational level, net operating working capital can be calculated as:

Operating net working capital (NWC) = debtors + raw materials + work in progress + inventory – creditors.

The lag between buying and holding inventory, making a sale, and finally collecting cash and settling creditors creates a timing difference between profit and cash flow.

Working capital absorption is typically the main reconciling difference between accounting profit and operating cashflow.

This difference fundamentally drives what analysts and market commentators call the quality of a company's earnings. When a business grows rapidly, the timing difference between recognising profit and generating positive cash flow can create cash flow or liquidity problems for management.

This is due to costs associated with inventory that require payment in advance of making a sale. If the sale is made on credit terms, it takes longer to collect the cash.

Depending on the industry, this cycle could take more than ninety days, meaning the business must fund this timing difference.



Our perspective

The essence of working capital management is being able to actively manage working capital within an optimal range to keep pace with the company's scale of operations. This can be accomplished by right-sizing current assets and liabilities on the balance sheet to optimise the operational capital employed in the business.

CASH TO CASH CYCLE

When working capital is expressed in days, it is commonly called the cash conversion cycle or cash-to-cash cycle (C2C).

The C2C cycle reflects the time in days it takes a company to convert sales to cash.

The operating NWC positions are translated into 'days outstanding', which is the number of days cash is tied up in inventory and receivables or financed by the suppliers in accounts payable.

It is defined as follows:

$$\text{C2C} = \text{DIO} + \text{DSO} - \text{DPO}$$

- **Days inventories outstanding (DIO)** = average number of days that inventory is held.
- **Days sales outstanding (DSO)** = average number of days until a company is paid by its customers.
- **Days payables outstanding (DPO)** = average number of days until a company pays its suppliers.

WORKING CAPITAL MANAGEMENT AND STRATEGY

The C2C cycle can be analysed and viewed in light of a company's strategy. A business that competes as the lowest-cost supplier should have tight working capital policies and manage its inventory and receivables days with discipline, including short credit terms and the willingness to accept stock-outs to avoid holding excess inventory.

Alternatively, a niche player is more inclined to extend favourable credit terms and hold more inventory lines to reflect a business model that charges higher prices to its customers.



Our perspective

Working capital management aims to ensure a company can continue its operations and generate sufficient cash to satisfy cash requirements for operational expenses, service debt, and return dividends to shareholders.

How well do you approach working capital management?

Management teams are typically rewarded for their ability to hit budgets and forecasts based on profitability hurdles. Many companies don't have express productivity targets for working capital efficiency and rarely set targets and benchmarks for working capital management while providing the right people with incentives.

CHECKLIST FOR MANAGEMENT

- Do you set targets for payables, stock and debtor management?
- Are your management team incentivised to achieve improvements?
- Are customers incentivised to settle in cash?
- Do you have a long, lazy tail of slow-moving stock?
- Do you forecast demand and variability at the individual SKU level?
- Have you linked your forecasting system to planning and procurement systems?
- Do you have favourable terms with suppliers in your industry?
- Does your purchasing team receive kickbacks or incentives from suppliers?
- Do you adjust your forward ordering process based on experience?
- Are overdue accounts under control?
- Do you utilise direct debit and or other settlement facilities?
- Do you collect debts in a timeframe equal to or better than industry standard?
- Do you segment and classify stock items based on product lifecycles?
- Do you invoice on a regular and timely basis?
- Do you apply the same rigour and discipline to managing working capital as you do with the profit and loss?
- Do you understand the actual costs of holding inventory and set a target for inventory on the balance sheet?



Our perspective

Results will only be tangible when the leadership team applies the same focus, rigour, and discipline as managing the profit and loss statement to the balance sheet.

THERE IS A CLEAR LINK BETWEEN WORKING CAPITAL MANAGEMENT AND VALUE CREATION

Creating business value is all about generating returns that exceed the level of risk taken. Cash is said to be king, and investors and shareholders value growth in their investments. Therefore, business value can be expressed as a function of three inputs: free cash flow, risk, and growth.

Value = Free cash flow (FCF)/Risk less growth

Given the above valuation mechanic, there are three general options available to management for increasing the value of a company:

01

Increase the cash flow available to debt and equity providers (FCF)

02

Lower risk for the same reward

03

Increase the rate of growth

THE INTERPLAY BETWEEN WORKING CAPITAL ABSORPTION AND VALUE: WORKED EXAMPLE

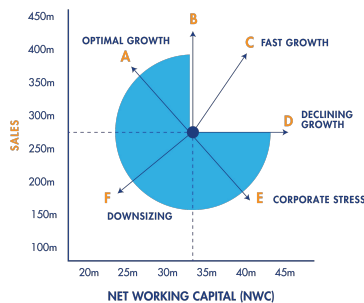
Assume a company generates \$1,000 in free cash flow, \$900 in Earnings before Interest, Tax, Depreciation and Amortisation (EBITDA), risk as measured by the company's cost of capital is 18%, and based on history, the future growth rate is expected to be 3% p.a.

Using the above valuation framework, the company could be valued at \$6,667. ($\$1,000 / (18\% - 3\%) = \$6,667$ or 7.4 times EBITDA.

Assume the business improves the rate of working capital being absorbed into it and now generates \$1,300 in free cash flow, with risk, growth, and EBITDA being constant.

The valuation framework would produce a valuation of \$8,667, calculated as ($\$1,300 / (18\% - 3\%) = \$8,667$ or 9.6 times EBITDA. In this simple example, management can increase a company's value through operating efficiencies focused on working capital improvements.

NETWORKING CAPITAL ABSORPTION



Our perspective

Increased efficiencies will lower the capital invested in the company, allowing surplus cash to be distributed back to shareholders or the additional free cash flow to be re-invested in strategic initiatives. Businesses with inefficient working capital management are often acquired at a relative discount.

Cash is King



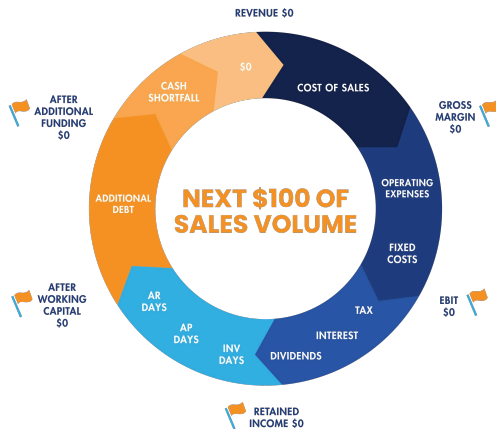
EBITDA is a financial measure widely used for financial statement analysis, credit assessments, valuations and as a proxy for cash flow. However, EBITDA has many shortcomings, and as the above example shows, EBITDA may not correlate to cash flow. One reason for this is that companies in different industries experience varying cash conversion cycles due to differing working capital requirements.

In this framework, we use the term free cash flow to mean the cash flow generated by the company’s operations, less any increase in working capital and investment back into the business. It is the cash flow the business generates before the service of debt in interest payments and the rewards to equity providers in the form of dividends. Therefore, free cash flow is the cash flow available to debt and equity providers and is independent of leverage.

LIQUIDITY MEASURES CAN BE FOOL’S GOLD

Traditional liquidity measures, including current and quick ratios, can mask systemic working capital issues. The current ratio, as measured by the level of current assets compared to current liabilities, has historically been accepted as favourable when it exceeds a ratio of 2 to 1. However, this measurement can be misleading if the company has a poor record of collecting debts and/or accumulating slow-moving and obsolete inventory.

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A HOLISTIC APPROACH

The financial report’s primary statements—profit and loss, balance sheet, and cash flow statement—were designed as a trilogy, meaning they are equally important and should be viewed and interpreted as such. Business wisdom comes from understanding the interplay and relationships between the three statements, not just one or two metrics.



Reverse engineering – debtors

Debtors in a business are typically monitored and managed using a profile of aged receivables that segments debtors based on the number of days outstanding, normally being current, 30, 60, 90 and 120 days past due.

At the company level, debtors days is commonly calculated by the following formula:

Days sales outstanding (DSO) = Accounts receivable/sales x days in the period

Consider an importing business with annual sales of \$250 million and an accounts receivable balance of \$50 million at year-end. Days sales outstanding (DSO) can be calculated as follows: $\$50 / \$250 \times 365 = 73$ days of unpaid credit sales at the end of the period. Suppose the importing business reduces the DSO from 73 to 45 days. In that case, the potential to free up cash can be calculated as follows:

Potential to free cash (DSO) = Current accounts receivable balance - (Sales/days in period x target collection terms)

Potential to free cash (DSO) = $\$50,000,000 - (\$250,000,000 / 365 \times 45) = \$50,000,000 - \$30,821,918 = \$19,178,082$

COMMON COLLECTION TEAM MISTAKES

01

No credit policy

02

No reference checks

03

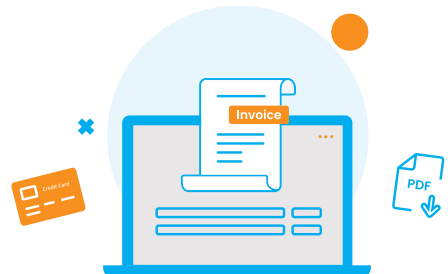
No progress payments

04

Not incentivising collections

05

No standard suppliers terms & conditions

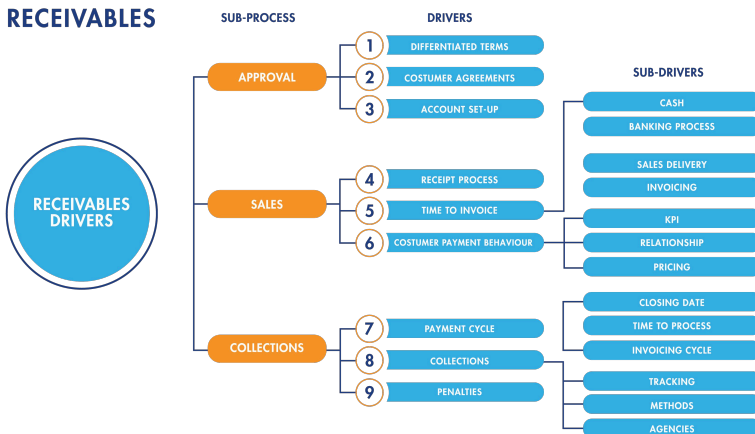


Our perspective

In this case study, collecting debts on average in 45 days instead of 73 days would free up approximately \$19.2 million in cash, which could be returned to shareholders or used to retire debt.

TEN IMPROVEMENT INITIATIVES TO IMPROVE MANAGING DEBTORS

- 01** Get organised and set goals, and address resourcing, accountability, and motivation of the team. Provide clarity on the role of the credit manager and the interplay between the billing system, procedures and the accounting function.
- 02** Determine the typical reasons debtors avoid payment. Adopt standardised counter tactics for dealing with common excuses for non- or delayed payment.
- 03** Review invoicing procedures to ensure that invoicing for long-term projects and recurring billing is done in advance. Adjust the billing cycle mix to minimise the impact of customer payment behaviour.
- 04** Ensure that the remuneration of sales staff is tied to appropriate sales measures and collection results.
- 05** Benchmark credit terms, pricing, and payment structures against competitors. Formulate a clear credit policy for extending credit and credit limits and extend payment terms that benefit your business and customers.
- 06** Enforce a disciplined process for assessing credit applications and performing background checks.
- 07** Set a minimum level of preparation before making phone calls and train staff on telephone tactics to counteract debtor habits and excuses.
- 08** Educate your staff and customers on how you want to be paid to get your bills paid as a priority.
- 09** Review the dunning process, including written communications and correspondence, including reminder letters, statements, invoices, letters of demands, and deeds of releases. Understand your rights and when to enforce them.
- 10** Consider using direct debits, early settlement discounts, late fees, debtor or invoice financing, and factoring.



Reverse engineering – creditors

Creditors, like debtors in a business, are typically monitored and managed using a profile of aged payables that segments creditors based on the number of days outstanding, typically being current, 30, 60, 90, and 120 days past due.

At the company level, days payables outstanding (DPO) are commonly calculated using the formula:

Consider an importing business with a cost of goods sold of \$250 million and an accounts payable balance at year-end of \$22 million. The days payables outstanding (DPO) can be calculated as follows:

$$\$22 / \$250 \times 365 = 32 \text{ days.}$$

If the importing business increases the creditors' days by 28 days, representing 60 days credit terms, the potential to free up cash can be calculated as follows:

Potential to free cash (DPO) = (Cost of Sales / Days in Period x Target Settlement Terms) - Existing Accounts Payable Balance

$$\text{Potential to free cash (DPO)} = (\$250,000,000 / 365 \times 60) - \$22,000,000 = \$19,095,890$$

However, it's worth noting that the days it takes to pay creditors often depend on the working capital management philosophy. Some companies deliberately defer settlement or stretch creditors to reserve cash. Other businesses may pay creditors quickly to achieve favourable return service and maintain a reputation in the local markets in which they operate.

COMMON MISTAKES

01

Settling creditors too quickly

02

Limited negotiation skills and focus on terms from buyers

03

Limited controls on the interface between vendor master files and online payment systems

04

No centralised procurement function



Our perspective

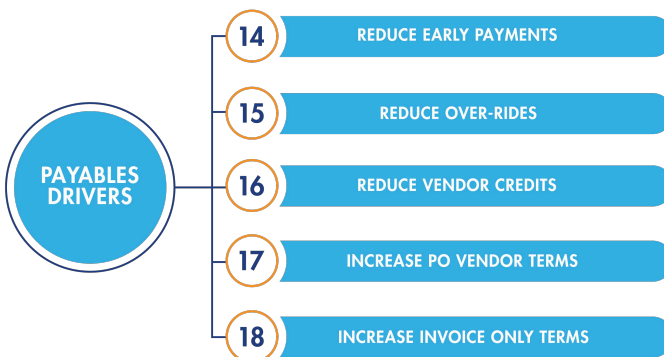
In this case study, extending payment terms from 32 days to 60 days would free up approximately \$19.1 million in cash, which could be returned to shareholders or used to retire debt.

TEN IMPROVEMENT INITIATIVES TO IMPROVE MANAGING CREDITORS

- 01 Determine whether payment of existing creditors can be extended or the outstanding amount can be paid in instalments. Balance this against enhancing and maintaining your credit rating and quality.
- 02 Review supplier arrangements to obtain more favourable payment terms (e.g., discounts for prompt payments and extended credit terms).
- 03 Review authorisation procedures and policies to ensure that discretionary expenditure is adequately controlled.
- 04 Consider centralising the procurement function to unlock volume-based discounts.
- 05 Segregate and segment suppliers based on attractiveness and relative value of the business to drive negotiation approaches and tactics.
- 06 Perform a cost-benefit analysis to model the benefit of taking advantage of early settlement discounts rather than deferring payments.
- 07 Consider using professional advisors when dealing with the Australian taxation office.
- 08 Ensure purchase orders cover the majority of supplier spend.
- 09 Review the security for online banking controls, including access, monitoring, segregation of duties, vendor master file security and logical access.
- 10 Perform GST and key supplier integrity checks to identify incorrect or duplicate invoices

PAYABLES

DRIVERS



Reverse engineering – inventory

Depending on the industry, inventory can be the largest component of working capital that ties cash up. If inventory is not turned over regularly, it incurs overheads such as storage, administration, handling and insurance. It is also subject to risk of damage, theft, deterioration, obsolescence and may even be perishable. The amount of inventory held at any time depends on balancing the holding costs against the opportunity cost of stockouts. Therefore, deciding when an operation should replenish its inventory is a critical success factor. From our experience, many companies overstock simply by purchasing goods greater than historical usage, which leads to excess working capital. At the company level, the number of days inventories outstanding (DIO) is a commonly used key performance indicator and is calculated by the following formula:

Days inventories outstanding (DIO) = inventory/cost of sales x days in the period

Consider an importing business with a cost of goods sold of \$250 million and stock on hand at year-end of \$75 million. The days inventories outstanding (DIO) can be calculated as follows: $\$75 / \$250 \times 365 = 109$ days.

If the importing business decreases the inventory days by 21 days, representing 88 days' worth of stock, the potential to free up cash can be calculated as follows:

Potential to free cash (DIO) = Stock on Hand - (Cost of Sales / Days in Period x Target Inventory Days)

Potential to free cash (DIO) =
 $\$75,000,000 - (\$250,000,000 / 365 \times 88)$
 $= \$75,000,000 - \$60,273,973 =$
 $\$14,726,027$



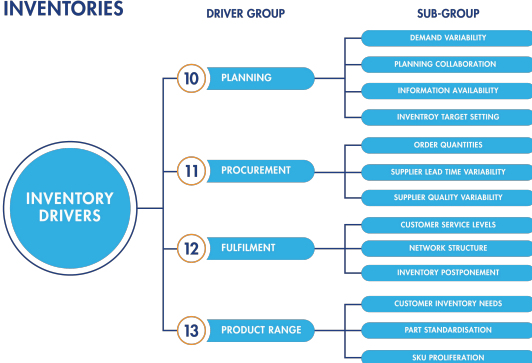
Our perspective

In this case study, reducing inventory days from 109 days to 88 days would free up approximately \$14.7 million in cash, which could be returned to shareholders or used to retire debt.

TEN IMPROVEMENT INITIATIVES TO IMPROVE MANAGING INVENTORY

















- 01 Benchmark key performance indicators such as stock turns and inventory days against competitors. Clarify roles and responsibilities, set targets, incentivise the team and monitor accordingly.
- 02 Regularly review slow-moving inventory items and obsolete stock (dead stock). Consider selling such items at a discounted price to generate cash flow. Clearing houses and auctioneers can facilitate clearances of long, lazy-tail products.
- 03 Review inventory processes and policies including valuation policy, stock take procedures and provisioning policy.
- 04 Review the production and procurement cycles to ensure that scrap/ wastage and work in progress are minimised.
- 05 Conduct a stock-keeping unit (SKU) analysis to determine if the product range required to be stocked can be rationalised by eliminating redundant and slow-moving SKUs.
- 06 Where possible, standardise all or part of the product range or inputs.
- 07 Evaluate the benefits of switching from make-to-stock to make-to-order.
- 08 Optimise batch sizes, review warehouse planning and utilisation, distribution network and retention of title clauses.
- 09 Adopt a disciplined and analytical approach to forecasting and demand planning tasks using statistical analysis to track purchases versus sales or usage. Track stock-outs and minimise frequency.
- 10 Simplify and integrate IT platforms into sales and operations planning, forward ordering and stock management

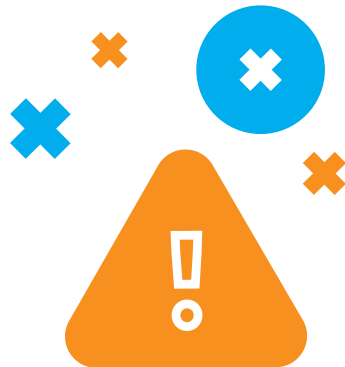
INVENTORIES



Working Capital red flags

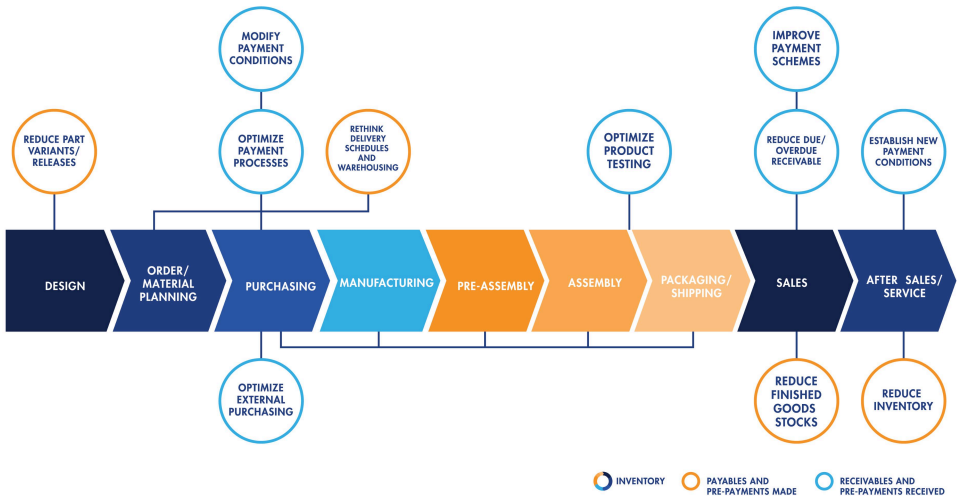
How do I know if I have a problem? - Common indicators and triggers for a working capital review

-  The business is generating strong sales but never seem to have enough money.
-  The business has a deteriorating cash position.
-  Working capital metrics and lack of accountability.
-  You have difficulties in managing seasonal fluctuations.
-  You find yourself regularly bumping up against credit limits.
-  There is an inability to fund future capital expenditure needs from operations.
-  You have invested in new systems, but your cash management performance hasn't improved.
-  Your bankers are suggesting you review your operations.
-  You never know what your cash position is.
-  You have large differences between profit and cash flow.
-  You have large amounts of money that are tied up in capital.
-  Your bank overdraft and operating finance lines are drawn down.
-  You are approaching or have breached bank covenants.
-  You experience difficulty in raising additional capital.
-  You are planning to sell the business in the future.
-  You are experiencing high levels of working capital investment compared to sales revenue



Summary

The most successful companies apply the same discipline to capital management as they do to the profit and loss account. They understand the C2C value chain and working capital levers and actively address the root causes of tied-up cash, making the company more valuable for shareholders.



BENEFITS OF DISCIPLINED WORKING CAPITAL MANAGEMENT

Increasing cash flow will enable you to reduce the capital intensity of your business, which means you will increase the return or yield the business generates on its capital as measured by return on capital employed (RoCE) or Economic Value added (EVA) analysis.

Increasing free cash flow in the business will also make the company more valuable as measured by enterprise valuation models based on discounted cash flow techniques. This means the business will be worth more, allowing management to extract additional value on exit. Freeing up additional cash also gives management more options, including:

01

The increased ability to pay higher dividends.

02

The ability to pay down additional debt to reduce finance charges and increase net operating profit.

03

Improved credit rating and increased capacity to borrow and service additional debt to fund future growth.

04

The ability to re-invest in the businesses by additional capital expenditure and research and development.

05

The ability to pass on savings to customers to improve competitiveness and increase market share.



At Berkeley Advisory (BA), we've unlocked millions in cash for clients by optimising WCM. Our methodology blends analytics, operational expertise, and leadership alignment to transform your finance team into a strategic powerhouse.

Ready to turn WCM into a competitive edge and drive business value? Contact us today.



Contact us to find out how
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company into a market leader today.

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