THE DAVIDSON GRAY PODCAST

HOW TO MANAGE CASH IN YOUR RECRUITMENT BUSINESS

How to manage cash in your recruitment business Podcast Transcript

Hi, I'm Rhys Jones. Welcome to my introduction to cash management in your small recruitment business.

The challenges

This is an intro because cash management in your business is a massive subject. So this is one for people that are thinking a setting up, just set up, or in the first few years are quite frankly struggling with cash management because cash management is going to be alien to a recruitment consultant because you are used to being an employee and when you get your money, then it's net of tax. When you set up a business, you've got four taxes. You've got PAYE, corporation Tax, personal Tax, and VAT, and what makes it great, they all come at different times, so you can't budget that well.

And also what makes even harder within the first two years of business is your first corporation tax bill and first personal tax bill may not come for 12 months, 18 months, or even two years. It depends when you set up the business, but when you do get the bill, With a personal tax bill, you pay your personal tax bill on what you've earned, but also you have to pay some upfront for the following year so you come out with a massive bill.

So it is a big challenge. So when I speak to small businesses and mostly people that want to set up, cause that's obviously what I do for a living to say, how do you manage cash? You know, how much money should you have in the bank? How much should you save? And the problem is you've got that ongoing challenge as a business builder, because as a business builder, you use your money to make money. That's the whole point. So if you look at recruitment consultant, you're hiring someone doing 150 grand a year at 150 grand, you pay them 50. And then you've got 50, that's about a third of it that pays your operational costs. So that's the office costs, the desks, the phone, and then the people that don't bill.

Then you get 50-gun profit. So there you go. You're making your profit. Similarly with marketing, if you watched any of my marketing videos or blogs or read the blogs, you'll know you can make significant returns on investment with your marketing. So for example, if it's Google advertising, for every pound you make like five pound back.

So while you're growing your business, you want to use the money to make money. You can't run out money. If you run out money, you're knackered, you know, a bit like a car runs out a petrol, you know your business will stop. So you've got to manage that. So you've got all these bills to look after and you're investing in your growing business.

Find your breakeven point

So how do you do with that? One of the key things that you've got to get in your business is understanding your breakeven point. Now, your breakeven point is the average amount that, that it costs to run your business per month. Now I stress average. Don't look at your breaking point on a monthly basis, because it's going to vary.

Now when you are talking to an accountant, if you haven't got some internal in the business that can do this, ask them if they will do it for you. And what you're really looking at is preferably, I would say, a three month average, three month average of what you cast are over that period. But don't fall into the trap of excluding things that you think are exceptions because you will get exceptions, like say a new website or a direct fee.

The problem is you are always going to get exceptions. So if you ignore the exceptions, you're kidding yourself . So the way I would suggest it is when you look at your exceptions, so for example, a rec 2 rec fee and you forecast over the next 12 months, you're going to take two people from rec2rec and to make it easy, six grand per rec2rec fee.

So that's 12,000 pounds. So annualize it and it's a thousand pounds a month. So if you've got annual bills, then just divide it by the 12. I'll put it annually. If it's quarterly, it's divided by three. So that helps you. But also, like I said, don't ignore the ones that you think won't happen again. You will get the odd ones.

You just think, oh, that's infrequent, like for example, you're buying loads of desks for the office, and you think, well those desks going to ask me for a lifetime. Okay. But those things, they do come up. So you can't ignore it, you've got to know your breakeven point. Cause if you don't know your breakeven point, how can you decide how much money you've got in your bank account to cover if you have a bad period.

But also if you don't know your breakeven point, how would you know when you're making profit? And that's what it's all about, is making profit. So you've got to understand your breakeven point. So how do you manage your cash in a day-to-day basis? Well the vast majority of recruitment companies will work on a negotiated rate basis.

Manage your cash flow

So say your fee is 25% of your terms and you negotiate down to 20%. Get all your staff and do it yourself. When you agree that rate, say to the hiring manager, this is on the basis that you pay within terms. Now within your terms, it'll be 14 days or 28 days. Now your hiring manager, he or she will probably agree to that.

The vast majority you do, because it's not down to them. They're interested in hiring that person to work in their department. They don't work in the accounts department. They're not bothered. So they agree to that. Put it in writing. It's also in your terms as well, but when you send your invoice, make it loud and proud on your invoice.

So what you might even do is have the invoice amount and put discounted rate underneath it, put the rate that it will be at full terms, and you say discounted rate on proviso it's paid within terms of 14 days. Then ring the accounts department and talk to them and say, just making sure you've got the invoice.

Can you tell me when it's likely to be paid. I also want to make you aware there is a discounted rate based on payment within terms and that I'll get it right down. And this is tied into something called debtor days where you're looking to see how much it takes you on average to collect the cash. Cause you've got to be on top of the cash.

So not only have you got to know what bills are going out, you've got to make sure you collect your cash properly. Now, in the first few years of business I recommend working in an opposite way to bigger businesses. And what I mean by that is you pay your bills on time straight away.

So it means you haven't got bills hanging around that are going to catch you out. Because what is easy to do is agree payment plan on everything. Delayed payments or you just delay a bill and before you know it, your breaking point is getting bigger and bigger and bigger to the point it's getting harder and harder to make profit.

So let's say for example, you're always looking at the new tech. Now that's per month. It's easier to keep doing that, but then your breakeven point is getting bigger and bigger. So going back to paying on time, I found through experience that as a small business, it's important that you have suppliers to your business that you try and have a partnership relationship with.

Negotiate terms

You don't necessarily get it with bigger companies. Smaller companies, like say digital marketing companies for argument's sake. If you agree to pay them on time or even early or even up front, you usually get a very good discount. Now, one thing I did, it was when I negotiated the lease on our premises, quite a big premises.

It was a three-year lease. So I said to the landlord, I will pay you upfront every year, but I want a discount. He said, well, that's fine. Because he doesn't want me to do a runner. I manage to get a 30% discount from paying upfront and, which is absolutely ridiculous. If you think. If I'd borrow the money from the bank to pay him, that wouldn't have cost me 30%.

But I've got a massive discount and so, I think it helps to pay your suppliers on time and keep on top of your bills. Now, going back to your three bills. You've got your VAT, your corporation tax, your PAYE, your personal tax. There's one bill. You've got to be dead careful of VAT. Now, VAT is basically you are collecting cash on behalf of the government.

Don’t mess with the VAT-man

It's their money. So don't think you can't pay them because they will see their ass. You know, with corporation tax bills, they will be sympathetic if you're struggling. You can have payment plans. PAYE could be the same as well. But VAT just don't, just don't fuck with them. The VAT man can be on top of you.

So make sure you pay your VAT. So when you get your cash that lands at the bank, because you're not used to cash management, you've got 20% on top of that, which is for the VAT man, which you can see in the account, you think it's yours, but it's not yours. It's a loan from the VAT man, so you make sure you keep that to one side . So when we're going back to the conversation to have with startups is how much money do you want to keep in the bank account?

This is where it's difficult because you've got that using the money to make money. But also what I do highly recommend is you use your breakeven point as a hard and fast guideline that you have, let's say for arguments' sake, a minimum of a month's break even in your bank at any point in time. So if you have a really shit month you've got money in the account, you might want to have two months in the bank account. You might want to have three months in the bank account. That depends on your risk profile, how aggressive your plan is. And if you've got a sympathetic partner investor, like for example, you know, Davidson Gray, you know if, if the business is going through some massive expansion, we are there to help you out with cash.

Don’t get carried away

That's what we'll do. So if you've got someone that can help you, that's fine, but just be careful. Don't get too carried away. You've got to be sensible with your money. The natural tendency of recruiters is to be ambitious because that's what makes you good. But you can be over ambitious in your growth with your spend.

Now, your growth plan can be really ambitious. That's great. But you've always got to make sure that your cash management is sensible and it's safe. And this is where I would say that, you know, one of your first hires within your business, so you first support hires, or your admin hires, whatever it might be.

Try and get somebody who is good with cash. Somebody who is good with numbers, somebody who maybe understands it a bit, somebody who could work with that, because you've got so many things to run in your business here. You've got vacancies coming in, you got candidates coming in. You're trying to attract staff to work for you, you' re managing the staff that work for you.

You might even still be billing. So all these things, you've got to manage the marketing as well. So when it comes to the cash management and managing the accounts, that's a detailed thing. So you've got to stay on top of it, but you probably will be reluctant because the vast majority of recruiters I speak to don't like accounts, don't want anything to do with accounts, don't understand them.

I'd rather have a problem, take it away, which is what we do at Davidson Gray. But, if you hire somebody in your business that can do that, they can stay on top of your account and that's where they can stay on top of the breakeven, if it changes, you need to know. But also, it's managing bills month to month because you will get some of the bills that will grow.

Let's say job adverts, it might be LinkedIn license. You've got to keep on top of where something's gone wrong. You know, where there's a massive overspend somewhere. It might be that there's somebody that's gone crazy on LinkedIn adverts or, on job boards.

The importance of budget and variance analysis

So there's one thing that I recommend that you do when you've got that support staff is something called a budget and variance analysis. What you do is, is you look over, there's a three month breakeven point, and you look at what you spend on average for each thing and especially the annualized stuff.

So you can see what your average is. Now when your admin person does the report, they can compare against what the average should be, what it was for that month. Now if anything sticks out, they look into it. So if anything's dropped massively, look into it. Anything that's gone up massively, definitely look into it and see the reason for it.

So they can spot the problem immediately. Then you can address it straight away. Because if you are not on top of your numbers of which you've got so much else to consider at the same time, then it's easy. Stuff can start slipping through. Overspend can start slipping through. So you've got to keep on top of that.

Especially, I look at new tech, because there's always new tech out there that help you with the recruitment business, which I definitely advocate you having in your business, but not doing the whole, we'll get that page one placement because you can get carried away with it. And also you can get to the point where your breakeven point becomes that high you can't make profit.

But if you've got somebody in the business that's looking at your budget and variance analysis, you can say, you can see if anything sticks out that's odd so you can address it straight away. So the whole cash management situation of a business in the first few years, it is complicated, and it can be confusing and it can be worrying, but one of the big benefits of setting up your recruitment company is it's not necessarily a big cash drain.

Staff - your biggest spend

You don't have to buy products, you haven't got warehouses. You know, you haven't got the spend that most businesses have because your biggest spend within your business is yourself. Obviously, you're paying yourself and your staff. That's the biggest thing, is actually paying your staff.

Now, if you're managing your staff, correctly, you are only paying staff that are making you money, which might sound obvious, but you can get carried away with staffing up quickly and hiring people on the basis that they're going to bill. And that's when you can get into an area of what I call vanity hires and vanity numbers, where you've got a lot of staff in your business.

You think, great, I've got a 10 person business, I'm doing really well, but they're not making that much money. And it's all vanity. You know, it's placements, vanity, invoices, sanity, cash is king. Don't get too caught up with hiring too quickly cause you're making cash. Because with a recruitment business, you shouldn't really get into cash problems because if you look at, like say an average biller, let's say 150 grand, 200 grand, there's a lot of profit in that.

If you set up your own recruitment business, you should be a good biller. So there should be a lot of profit in that. So there shouldn't really be that much of an issue. You know, the biggest costs are always paying people. If people aren't billing that much, you're not paying lots of commission.

So it shouldn't be an issue. It does happen in the first, you know, like I say, the first two years, four out of five business go bust because largely it's cash management. So it's that balancing at. I do strongly advocate if you can have somebody that you can turn to, a non-exec or a peer or somebody that understands business that you can chat to about the growth plans for your business, about the investments in your business so you can make sure you get the balance right, cause clearly you want to grow your business.

Cause if you are going to get to the point where you're working on the business rather than in it, the business is making money for you. You are not necessarily making the cash. That's where the value is. Then you need to invest in your business to grow it. But if you're going to invest in your business, then you've got that argument about okay, cash management.

Conclusion

So as much as any first few years you might say, okay, I want to keep all my corporation tax and all my personal tax to one side to make sure when I get the bill, I can pay it. That is going to hold your growth back. So it's a constant ongoing challenge. Maybe I'm making it sound more complicated than it is, but it's something you have to be aware of and it's something you've got to be conscious of.

And it's a skill you've got to learn as you grow your business is how to manage that return on investment without taking on too much risk. Because if you've taken on too much risk, things can go wrong. Don't think it's always going to be fantastic. Inevitably, every single business at some point has a shit period.

You know, something would go wrong, maybe something in the worldwide economy. Just be aware that it won't always be sunshine. You know, you've got to be aware of that. But as I said few moments ago, you shouldn't have a problem with running a recruitment business because there's not lots of big cash challenges.

You don't have lots of stock. You don't necessarily have big warehouses; you don't have production machinery. It's not rocket science, so you should be fine with it. So anyway, I hope you've enjoyed this introduction to cash management. If you have, make sure you hit the subscribe button. Thank you for watching.