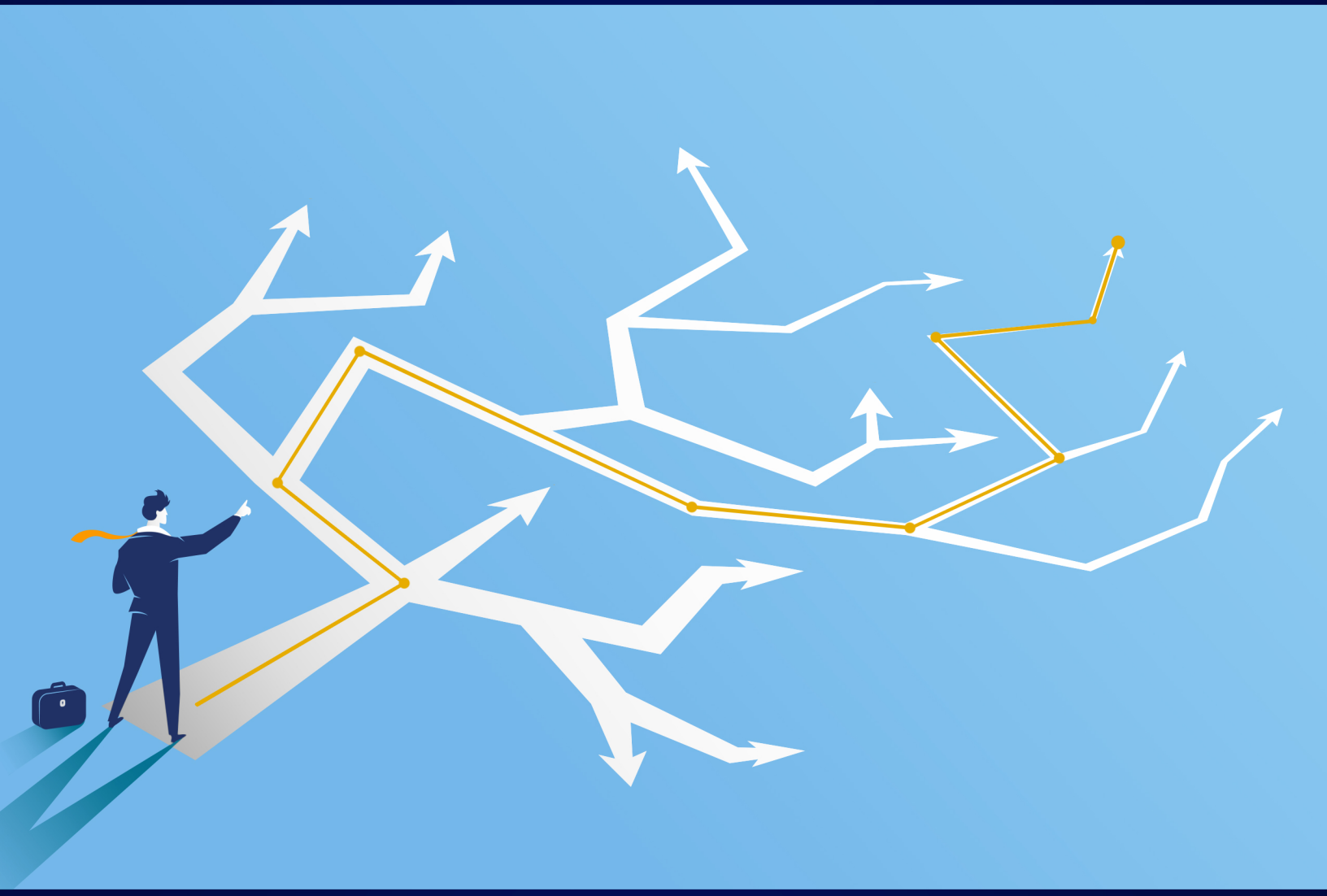
# MOST SMBs DON'T HAVE A CASH FLOW PROBLEM

# THEY HAVE A DECISION PROBLEM

## HOW BETTER BUSINESS DECISIONS CREATE STRONGER CASH FLOW—AND MORE OPTIONS



CASH FLOW DOESN'T HAPPEN BY ACCIDENT. IT REFLECTS THE CUMULATIVE IMPACT OF DECISIONS MADE THROUGHOUT THE BUSINESS—FROM GROWTH, PRICING, AND COSTS TO WORKING CAPITAL, CAPITAL INVESTMENT, DEBT, AND OWNER DISTRIBUTIONS. BETTER DECISIONS CAN CREATE STRONGER CASH FLOW. STRONGER CASH FLOW CAN CREATE MORE OPTIONS.

ROBERT S LIVINGTON

# MOST SMBs DON'T HAVE A CASH FLOW PROBLEM™

## THEY HAVE A DECISION PROBLEM

**How Better Business Decisions Create Stronger Cash Flow—and More Options**

**Robert S. Livingston**
**BusinessWiser™**

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This publication is provided for educational and informational purposes only. It does not constitute legal, financial, tax, accounting, investment, or other professional advice.

The concepts and observations presented are intended to help owners of small and mid-sized businesses think more broadly about the relationship between business decisions and cash flow.

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Business decisions are made under uncertainty. Even well-considered decisions can produce disappointing outcomes, while results are influenced by market conditions, competitive dynamics, management execution, financial capacity, timing, and numerous other factors beyond the author's control.

The premise of this Executive Guide is not that better decisions guarantee stronger cash flow.

It is that business decisions collectively influence the cash flow a business ultimately experiences—and that greater awareness of those consequences can contribute to more disciplined management.

## Professional Status & Experience Background

The perspectives presented in this Executive Guide reflect more than four decades of experience across financial, operating, executive, entrepreneurial, and owner-led business environments.

They were further informed by seven years of structured work with owner-led product businesses, including more than 50 consulting clients and approximately 120 members of the former BusinessWiser™ Advisory Circle.

Effective December 31, 2025, I formally concluded my consulting practice and Advisory Circle activities.

BusinessWiser™ now operates as an educational publishing platform. Its Executive Guides, Executive Tools, frameworks, and other resources are designed to strengthen business thinking, financial visibility, decision-making discipline, and cash flow management. They are not consulting or advisory engagements.

Stories and business situations referenced throughout this Executive Guide are drawn from historical experience across different companies, industries, economic environments, and periods of time. They are included to illustrate business principles and perspectives, not to suggest that another business should expect identical circumstances or results.

## Stories, Examples & Illustrative Scenarios

This Executive Guide includes stories, observations, examples, and business scenarios drawn from decades of real-world experience.

Where specific business situations are discussed, they reflect circumstances within particular organizations and periods of time. Certain details may be generalized where appropriate to focus on the underlying business principle.

Examples are provided for educational illustration only.

They are not presented as formulas, prescriptions, or guarantees that similar decisions will produce similar outcomes in another business.

The purpose of the examples is to demonstrate how decisions involving growth, pricing, costs, operating expenses, working capital, capital investment, debt, and owner distributions can ultimately become visible in cash flow.

Every business operates under different circumstances.

The objective is not to prescribe the decision.

**It is to improve the thinking behind it.**

# INTRODUCTION

# The Cash Flow Problem That Started Before the Cash Ran Out

### The Phone Call

It was Sunday afternoon, February 14, 1988—Valentine's Day—and I had been in my new CFO position for approximately one week.

Only days earlier, I had left a comfortable position as Vice President of Finance at what was then the second-largest floral wire service and gift-container company in the world. I had taken the new position because I wanted the challenge of helping turn around a struggling natural-food snack-bar manufacturer and, if we could put the business on stronger footing, help take it beyond the health-food industry and into the mass market.

I knew I wasn't walking into an easy situation. That was part of what attracted me to the opportunity.

My career to that point had prepared me for a great many financial challenges. I had worked in financial roles at Mobil Oil, Mattel, and Taco Bell, which was then part of PepsiCo. At Taco Bell, I had served as Manager of Financial Analysis and Cash Manager with responsibility involving approximately $250 million.

I understood financial management, banking relationships, cash forecasting, and the importance of maintaining liquidity.

What I had never personally experienced was a business that simply did not have enough cash to meet one of its most basic obligations.

That changed with a phone call late that Sunday afternoon.

The Controller had been working through the weekend, going through the company's numbers, when he called with the news no new CFO wants to hear.

“We can't make payroll next Friday.”

Approximately 300 employees were expecting to be paid. The company did not have enough cash to cover the payroll, and the available borrowing capacity was essentially exhausted.

Whatever ideas I may have had about how I would spend my first several weeks getting to know the company suddenly became secondary to a much more immediate problem.

We had five days to figure out how to make payroll.

Anyone who has led a business through a serious liquidity problem understands how quickly priorities change when there isn't enough cash. Strategic plans, growth initiatives, operating improvements, and longer-term investments may still matter, but they suddenly become secondary to obligations that cannot simply be postponed.

Those 300 employees had done their jobs with the expectation that they would be paid. Behind them were families with mortgages, rent, groceries, car payments, utilities, and financial obligations of their own.

Friday was coming whether we were financially prepared for it or not.

The obvious question that Sunday afternoon was:

**Where are we going to find the cash?**

That was the question we had to answer immediately.

But it was not the question that stayed with me for the next four decades.

That question was:

**How did the company get here?**

## The Problem Didn't Start That Sunday

The Controller's phone call made the problem impossible to ignore.

It did not create the problem.

A business rarely arrives at the point where it cannot make payroll because of something that happened a few hours earlier. The bank balance may reveal the problem on a particular day, but the financial condition behind that balance has generally been developing through decisions, commitments, operating results, and circumstances that occurred over a much longer period.

Before I received that phone call, inventory had already been purchased. Products had already been sold at particular prices and under particular payment terms. Employees had already been hired, expenses had already been incurred, and capital had already been committed. Growth decisions had been made. Financing decisions had been made. Borrowing capacity had already been consumed.

By Sunday afternoon, much of the story behind Friday's cash position had already been written.

That does not mean every decision leading to a cash-flow problem was necessarily a bad decision.

Some may have been entirely appropriate. Others may have been questionable in hindsight. Still others may have been necessary responses to customer requirements, supplier demands, competitive pressures, growth expectations, or operating circumstances management could not fully control.

Businesses do not operate in controlled environments. Customers change. Markets shift. Costs move. Suppliers encounter problems. Competitors react. Forecasts turn out to be wrong. Unexpected events occur.

That is why I have never found it particularly useful to begin with the assumption that a cash-flow problem means somebody must have made a terrible decision.

Sometimes there is an obvious mistake.

Often there isn't.

The more useful observation is that the cash position a business experiences today reflects decisions, commitments, operating performance, and circumstances that began developing before the result became visible.

When payroll is due Friday, of course, management still has to deal with Friday. There is no strategic insight profound enough to eliminate an immediate need for cash. The company may have to accelerate collections, negotiate with suppliers, work with lenders, postpone expenditures, inject capital, or find some other way to meet its obligations.

Immediate liquidity problems require immediate action.

But once the immediate pressure has been addressed, leadership has another responsibility.

It needs to understand how the business got there.

Because solving today's cash shortage without understanding what created it can leave the underlying pattern completely unchanged.

That distinction eventually changed the way I thought about cash flow.

## Cash Flow Is Where the Results Become Visible

When owners look at financial reports, they see numbers.

Revenue.

Gross margin.

Operating expenses.

Inventory.

Receivables.

Accounts payable.

Capital expenditures.

Debt.

Cash.

Those numbers are important because they tell us something about what has happened financially.

But businesses do not operate as numbers.

Behind the numbers are decisions.

A price was established or negotiated.

A customer was pursued.

Payment terms were accepted.

Inventory was ordered.

People were hired.

Expenses were authorized.

Equipment was purchased.

Debt was assumed.

Growth was pursued.

Cash was distributed to owners.

Each decision was made for a reason, usually by someone trying to accomplish a legitimate business objective. Some decisions increased cash generation. Others required cash. Some created obligations immediately, while others created financial consequences that would not become visible for months.

Eventually, many of those consequences appeared in the financial results.

That is the distinction at the center of this book.

**Cash flow is not where the story begins.**

**It is where the financial results of the story become visible.**

Over the decades following that Valentine's Day phone call, my responsibilities expanded well beyond traditional finance. I worked across financial, operating, executive, and entrepreneurial roles and eventually spent seven years working directly with owner-led product businesses.

The more of the business I could see, the more obvious the pattern became.

What appeared on the financial statements as a cash-flow result frequently had roots in decisions made elsewhere in the company.

That led me to a different way of thinking about cash flow.

**Cash flow is not simply a financial result.**

**It is a management result.**

Finance plays an essential role in measuring, forecasting, reporting, and interpreting that result.

But the business creates it.

## Ten Places Where Decisions Become Financially Visible

Throughout this guide, we will examine ten areas that have a particularly important influence on cash flow in owner-led product businesses:

**Growth.**
**Pricing.**
**Cost of Goods Sold.**
**Operating Expenses.**
**Inventory.**
**Receivables.**
**Accounts Payable.**
**Capital Expenditures.**
**Debt.**
**Owner Distributions.**

I refer to these as the ten primary Cash Flow Drivers.

But this is not a book about how to optimize those ten drivers.

We are not going to turn pricing into a technical pricing lesson, inventory into an inventory-management system, receivables into a collections manual, or growth into a financial formula.

Those subjects matter, but they are not the purpose of this guide.

The ten drivers matter here because they give us places to look when we want to understand how business decisions eventually become financial results.

Inventory does not simply appear.

Receivables do not simply happen.

Margins do not move without something changing.

Operating expenses represent commitments the company has made.

Capital expenditures begin with investment decisions.

Debt reflects financing choices.

Owner distributions reflect decisions about where cash generated by the business will reside.

Growth itself reflects choices about customers, markets, products, people, inventory, capacity, and pace.

The financial report shows us the result.

Our objective is to look behind that result.

## A Different Question

When an owner says, "We have a cash-flow problem," the natural question is:

**How do we improve cash flow?**

There is nothing wrong with that question.

If the company is under financial pressure, it may be an urgent one.

But I believe there is another question that should come first:

**What decisions created the cash flow we're experiencing today?**

That question changes the direction of the conversation.

Instead of beginning with the bank account, it begins with the business.

If inventory has increased, what happened inside the business that caused it to increase?

If receivables have expanded, what commercial decisions preceded that expansion?

If margins have weakened, what changed in pricing, purchasing, product mix, customer mix, costs, or operations?

If operating expenses have moved ahead of expectations, what commitments were made and what assumptions supported them?

If growth is consuming more cash than anticipated, what did the business have to put in place before the resulting cash arrived?

The purpose is not to assign blame.

It is to understand cause and effect.

That distinction becomes especially important because business decisions rarely fit neatly into categories of good and bad.

A decision can make perfect sense from one perspective and still create consequences somewhere else. A decision can consume cash today and create substantial value tomorrow. A decision can improve one part of the business while increasing demands on another.

The objective is therefore not to make every decision based on its immediate effect on cash.

That would be just as misguided as ignoring cash altogether.

The objective is to make important decisions with greater visibility into their financial consequences.

## What This Guide Is—and Isn't

This is not a cash-flow textbook.

It is not a turnaround manual.

It is not a collection of cash-flow hacks.

And it is not an argument that businesses should avoid growth, inventory, hiring, capital investment, debt, or owner distributions simply because they use cash.

Businesses exist to deploy resources productively. Some of the best decisions an owner can make require substantial amounts of cash before the benefits appear.

Nor is this book intended to turn every manager into a financial expert or require Finance to approve every meaningful business decision.

The subject is broader.

This guide is about **management perspective**.

It is about learning to see the connection between the decisions being made throughout a business and the financial consequences those decisions can create.

That is why the ten Cash Flow Drivers will provide the economic backbone of our discussion without becoming a technical implementation system.

The question is not simply whether inventory is too high, receivables are too large, expenses are increasing, or growth is consuming cash.

The more useful question is:

**What decisions put us here?**

And then we need to turn that question around.

Today's cash flow reflects decisions and circumstances that have already occurred.

But another set of decisions is being made right now.

Prices are being negotiated.

Customers are being pursued.

Orders are being placed.

People are being hired.

Inventory is being built.

Investments are being approved.

Growth commitments are being made.

Those decisions are already beginning to shape the financial position the business will experience tomorrow.

Which leads to the second question that will run throughout this guide:

**What decisions are you making today that are creating tomorrow's cash flow?**

That is the shift I want this book to create.

From treating cash flow primarily as something Finance monitors after the fact to recognizing it as something the entire business influences through the decisions it makes every day.

Because most cash-flow problems do not begin when the cash runs out.

By then, you are seeing the result.

To understand the result, you have to understand the decisions that helped create it.

And that is where our discussion begins.

# CHAPTER 1

# Cash Flow Is a Management Result

## Cash Flow Doesn't Begin in Finance

For much of my career, cash flow was viewed through the same organizational lens that many businesses still use today.

Accounting records what happened. Finance analyzes the results, prepares forecasts, monitors liquidity, manages banking relationships, and helps leadership understand where the company stands financially. When cash becomes tight, attention naturally turns toward those functions because that is where the problem becomes most visible and where many of the immediate responses have to occur.

There is nothing wrong with that.

A capable Finance function is essential to a well-managed business, and good financial visibility becomes increasingly important as a company grows and becomes more complex.

The problem begins when responsibility for **understanding** cash flow becomes confused with responsibility for **creating** it.

Finance may be responsible for measuring and reporting cash flow, but many of the decisions that ultimately shape the result are made elsewhere in the business and often well before the financial consequence appears.

Sales establishes or negotiates prices and customer terms. Purchasing commits money to materials and inventory. Operations influences production levels, staffing, efficiency, service requirements, and resource needs. Management approves hiring, compensation, technology, and other operating commitments. Leadership makes decisions about growth and capital investment. Owners determine how much cash remains in the business and how much is distributed.

Finance may participate in many of those decisions, particularly in a well-managed company.

But Finance does not originate all of them.

Nor should it.

The people closest to customers, suppliers, production, employees, markets, and operations bring knowledge to those decisions that Finance cannot replace.

The broader management challenge is making sure that important decisions are made with visibility into their financial consequences.

That distinction matters because cash flow does not begin when Accounting records the transaction or when Finance updates the forecast.

By then, the company may already have committed itself economically.

A customer may already have been promised a certain price and payment terms. Inventory may already have been ordered. A new employee may already be on the payroll. Equipment may already have been purchased. A distribution may already have left the company.

The financial report records the consequences.

The decisions came first.

Once that becomes clear, cash flow stops looking like something a single department creates and begins looking more like what it actually is:

**A management result being shaped throughout the business.**

## The Business Is Creating Cash Consequences Every Day

Most decisions that affect cash flow are not described as cash-flow decisions when they are made.

They are business decisions.

A salesperson prepares a quote.

Purchasing commits to an order.

Operations adjusts production or inventory.

Management authorizes overtime.

A new employee is hired.

An equipment purchase is approved.

A customer receives extended payment terms.

None of those decisions is likely to appear on a meeting agenda under the heading **Cash Flow Decision**.

Yet each can influence the cash the business generates, consumes, retains, or requires.

That is important because management activity is continuous.

Decisions are being made every day, often by different people for different reasons and on different time horizons. Some create immediate cash consequences. Others establish commitments that will influence the business for months or years.

Consider something as ordinary as hiring.

Management may add an employee because the organization needs additional capability. The decision may be entirely appropriate. But once the employee begins work, the business has created a recurring financial commitment involving salary, payroll taxes, benefits, and perhaps systems, training, space, or supervision.

The decision is not wrong because it uses cash.

The point is that a decision made to solve an operating problem has also changed the company's financial requirements.

Inventory provides another simple example. The business may hold more product because management wants stronger customer service, supplier lead times have increased, or demand is expected to grow.

Again, the decision may be completely reasonable.

But the additional inventory represents cash that has been committed to one purpose and remains committed until the product moves through the business and ultimately returns as cash.

This is why cash flow is being shaped long before anyone opens a cash-flow report.

The report allows management to see the financial result.

The business has been creating that result through ordinary decisions all along.

Owner-led companies make this particularly important because decisions can happen quickly.

One of the strengths of an entrepreneurial business is its ability to respond without layers of bureaucracy. The owner may make a customer decision in the morning, approve an operating expense before lunch, discuss a supplier commitment in the afternoon, and authorize an investment before the day is over.

That speed can be a significant competitive advantage.

It also means the company can commit financial resources very quickly.

No single decision has to be unusually large or obviously risky for the cumulative financial effect to become meaningful.

And that brings us to another reason cash-flow outcomes can be difficult to understand after the fact.

Decisions accumulate.

## Decisions Accumulate

Major financial commitments tend to receive attention.

A new facility, a substantial equipment purchase, an acquisition, or a significant borrowing arrangement feels consequential. Management understands that a large amount of capital is being committed, so the decision usually receives appropriate scrutiny.

Many decisions affecting cash flow do not arrive with the same visibility.

They are smaller.

More frequent.

Easier to justify individually.

Their significance appears only after they accumulate.

A modest customer discount may have little effect on one transaction. If similar exceptions become common across a large amount of revenue, however, the combined effect on margin and cash generation can become meaningful.

The same thing can happen with inventory. One additional order may be entirely sensible. So may a small increase in safety stock, additional inventory for a new customer, or another SKU added to the product line. None necessarily creates a problem.

Over time, the business may nevertheless discover that substantially more cash has become committed to inventory even though nobody ever made one explicit decision to increase the investment by that total amount.

Operating expenses can evolve the same way.

A software subscription is added. Another position is approved. Marketing spending increases. Benefits improve. Professional services expand. Each commitment may have a reasonable business justification.

Individually, none appears transformative.

Collectively, they become part of the recurring economic structure of the company.

During my years working directly with owner-led product businesses, I saw variations of this pattern repeatedly. Owners would sometimes expect a meaningful change in cash flow to have one equally meaningful cause.

Sometimes it did.

Just as often, the financial result reflected the accumulated effect of many ordinary decisions made across the business over time.

That distinction matters because management can waste considerable effort looking for the one thing that went wrong when there may be no single event to identify.

The business may simply have been changing financially one decision at a time.

This is not an argument that small decisions require elaborate financial analysis.

That would make an owner-led company painfully slow.

It is an argument for recognizing that repetition changes significance.

A small decision made once may be immaterial.

The same decision repeated across customers, products, suppliers, employees, and months can become strategically important.

And accumulation becomes even harder to recognize because the decision and its cash consequence often do not occur at the same time.

## Yesterday's Decisions, Today's Cash Flow

Business decisions and their cash consequences rarely occur on exactly the same schedule.

That timing difference is one of the reasons an owner can look at today's bank balance and wonder why it does not seem consistent with what is happening elsewhere in the business.

Consider a product business.

Inventory may be purchased or manufactured weeks or months before it is sold. Once the sale occurs, the customer may not pay for another thirty, sixty, or ninety days. Cash therefore leaves the business well before the complete cash cycle returns it.

Hiring creates a similar lag.

Management may add people because growth is expected, because the organization needs capability, or because existing employees are stretched. Payroll begins immediately. The economic benefits management expects from the hire may develop over time.

A capital expenditure makes the timing difference even more obvious. A manufacturer may purchase equipment because it expects greater capacity, lower labor requirements, improved quality, or better efficiency. A large portion of the financial commitment may occur today while the benefits develop over several years.

Debt alters timing in another way. Borrowing can provide financial capacity immediately, but principal and interest obligations extend into the future.

Owner distributions work in the opposite direction. The owner receives value today, while the business operates tomorrow with less internally retained financial capacity than it otherwise would have had.

None of those timing differences makes the underlying decision good or bad.

They simply illustrate why the financial consequence of a decision may become visible well after the decision itself has been made.

Growth can make the effect particularly noticeable.

A company may report increasing sales and attractive profits while its bank balance tightens and borrowing increases. Those results can look contradictory until management considers the timing.

The company may have purchased inventory before making the sale, financed the receivable after the sale, hired people before the additional volume fully developed, and invested in additional capacity to support expected demand.

The economic benefits and the cash requirements are moving on different schedules.

This is why today's cash flow often contains yesterday's decisions.

Some were made last week.

Some last quarter.

Some may have been made years ago and gradually became part of how the company operates.

Management does not need to reconstruct every historical decision.

The more valuable insight is forward-looking.

If decisions made months ago are influencing the financial position today, then decisions being made today are already helping shape the financial position management will face months from now.

That realization moves cash-flow thinking upstream.

Instead of treating the current cash number as the beginning of the discussion, leadership starts viewing it as the result of a process that began earlier.

And once the owner sees that, the fundamental management question changes.

## The Owner's Question Changes

When cash becomes tight, owners understandably want action.

They want receivables collected, unnecessary spending reconsidered, inventory examined, payments managed, and financing alternatives explored.

Depending on the situation, every one of those responses may be appropriate.

A business facing an immediate liquidity problem cannot simply analyze causes while ignoring the need for cash.

But the management conversation should not stop with the immediate response.

If leadership treats cash flow only as a result to be corrected, the company can improve the short-term number without understanding the decisions and behaviors that produced it.

The pressure may ease.

Then return.

A different conversation begins when the owner asks:

**What decisions are producing the cash flow we're experiencing?**

That question does not assume those decisions were wrong.

It moves the discussion upstream.

It asks leadership to look beyond the financial result and become curious about what happened inside the business before the number moved.

The familiar question—

**How do we improve cash flow?**

—is not wrong.

It is incomplete.

The better management sequence is to understand what is creating the result before deciding what, if anything, should change.

That distinction is fundamental to this entire guide.

Finance remains essential. Management still needs reliable reporting, forecasting, analysis, liquidity management, and financial discipline.

But cash-flow management becomes broader than what Finance can accomplish after decisions have already been made.

The owner begins recognizing that the business is continually creating financial consequences through the way it sells, buys, operates, invests, grows, finances itself, and allocates the cash it generates.

That is the mental shift Chapter 1 needs to establish:

**Cash flow is not simply something Finance reports.**

**It is a management result.**

And once we accept that premise, the financial numbers themselves begin to look different.

An inventory increase, a margin change, a larger receivables balance, higher operating expenses, or additional debt no longer represents only a financial result.

Each becomes a clue that something happened somewhere in the business.

The number tells management **what** happened financially.

The next question is **why**.

And answering that question means looking for the decision behind the number.

# CHAPTER 2

# The Decision Behind the Number

## Numbers Tell You What Happened

Business owners live with numbers.

Revenue. Gross margin. Operating expenses. Inventory. Receivables. Accounts payable. Debt. Profit. Cash.

Those numbers provide essential information about what is happening inside a company. As a business grows, they become increasingly important because intuition and personal observation can no longer provide a complete picture of an organization that may include hundreds of customers, thousands of products, multiple suppliers, dozens of employees, and an expanding number of decisions being made every day.

I have spent much of my career working with financial information, and I would never minimize its importance. Good financial reporting gives leadership visibility that would otherwise be impossible. It allows management to compare performance over time, identify meaningful changes, test assumptions, recognize emerging problems, and determine whether the business is producing the economic results leadership expects.

Without reliable numbers, owners are often left managing through impressions.

And impressions become increasingly unreliable as complexity grows.

The limitation is not in the numbers themselves.

The limitation comes from expecting them to explain more than they can.

Suppose an owner reviews the monthly financial statements and sees that inventory has increased by $400,000 over the past six months.

That is important information. It tells management that substantially more of the company's financial resources are now committed to inventory than they were six months earlier.

What the number does not tell management is why the increase occurred.

Perhaps sales have grown rapidly and the additional inventory is necessary to support that growth. Perhaps the company added a major customer that requires certain products to remain continuously available. Supplier lead times may have lengthened, forcing Purchasing to order earlier. Management may have launched a new product family, or Operations may have increased safety stock after repeated shortages created service problems.

The same $400,000 increase can therefore describe very different business situations.

One may represent a sensible investment supporting profitable growth.

Another may reflect inventory accumulating faster than the business can sell it.

The accounting number is accurate in both cases.

What differs is the business story behind it.

Receivables provide another example. If accounts receivable rises by 25 or 30 percent, leadership needs to see the change. But the number by itself does not tell management whether sales increased by roughly the same amount, customers are paying more slowly, customer mix changed, or the company deliberately accepted longer payment terms to win larger accounts.

Again, the financial result is correct.

The interpretation depends on what happened inside the business.

The same distinction applies almost everywhere on the financial statements. A decline in gross margin tells management that the economics of sales changed. It does not, by itself, explain whether the cause was pricing, discounts, supplier costs, freight, product mix, customer mix, production efficiency, or some combination of them.

An increase in operating expenses tells leadership that the company is spending more. It does not say whether management added people ahead of growth, invested in technology, expanded facilities, increased marketing, or simply allowed spending to drift upward without sufficient scrutiny.

Numbers therefore tell management something indispensable:

**What happened financially.**

What they usually do not tell management completely is:

**Why it happened.**

That second question requires looking behind the number.

## Every Number Has a Story

Financial statements compress an enormous amount of business activity into relatively few categories.

Inventory may appear as one number.

Inside that number may be thousands of individual decisions involving forecasts, customer requirements, supplier lead times, order quantities, production runs, safety stock, new products, slow-moving items, and assumptions about future demand.

Accounts receivable may appear as one number.

Behind it are customers the company chose to serve, prices it negotiated, credit decisions it made, payment terms it accepted, exceptions it granted, invoices it issued, and the actual payment behavior of those customers.

Operating expenses may appear as one line—or several lines—on an income statement.

Behind them are decisions involving people, compensation, technology, facilities, marketing, insurance, professional services, and organizational infrastructure.

The financial statement has to compress those decisions because that is its job.

Its purpose is to provide a structured financial representation of what has happened in the business.

Management's job is different.

Management has to understand what the financial result actually means.

That distinction becomes increasingly important when the number changes meaningfully.

When I look at a financial result that has moved, I am usually interested in what changed inside the business before the number moved. Not because every change represents a problem, but because financial results rarely change without something else changing first.

Inventory did not decide to increase.

Receivables did not decide to stretch.

Operating expenses did not decide to grow.

Debt did not decide to appear on the balance sheet.

Something happened.

A customer was added.

Terms were changed.

A purchasing quantity increased.

A product line expanded.

People were hired.

Equipment was purchased.

Growth occurred more quickly—or more slowly—than expected.

Or perhaps an external circumstance changed something management did not control.

That last possibility matters.

The purpose of looking behind a financial number is not to force every result into a convenient story in which management caused everything that happened. Businesses operate in markets. Customers change their behavior. Suppliers increase prices. Interest rates move. Competitors act. Economic conditions shift.

Not every financial outcome can be traced neatly to a management decision.

But even when external events play an important role, management still needs to understand how those events interacted with the decisions already embedded in the business.

That is why I like the idea that every meaningful number has a story.

The number tells management where to look.

The story helps explain what management is actually looking at.

And without that distinction, leadership can easily respond to the visible financial condition while leaving the underlying cause untouched.

## Symptoms Versus Causes

When cash becomes constrained, the immediate financial condition deserves attention.

If receivables are large and customers are paying slowly, improving collections can generate cash.

If inventory has become excessive, reducing purchases and converting inventory into sales can release financial capacity over time.

If expenses are genuinely too high, reducing spending can improve future cash generation.

If the company faces a temporary liquidity requirement, borrowing may be completely appropriate.

These are real management actions addressing real financial conditions.

The problem arises when the immediate response becomes confused with the explanation for why the condition developed.

Consider a growing company that repeatedly relies more heavily on its line of credit.

Management may reasonably conclude that the business needs a larger credit facility.

That may be exactly right.

Growth frequently requires additional working capital, and external financing can be an appropriate source of that capital.

But suppose borrowing is increasing much faster than management expected.

The more important issue may no longer be simply the size of the credit line.

Perhaps inventory is growing faster than sales because the company continues adding products while older items move slowly. Larger customers may be negotiating longer payment terms. Margins may be weakening because pricing has not kept pace with supplier costs. The company may have hired people or expanded infrastructure based on growth assumptions that have developed more slowly than expected.

A larger credit facility may provide the liquidity necessary to support all of those commitments.

What it cannot determine is whether those commitments make economic sense.

That is the distinction between treating a symptom and understanding a cause.

Businesses can become remarkably effective at relieving financial pressure without changing what repeatedly creates it.

Cash tightens, so management focuses aggressively on collections. Several large customers pay, the pressure eases, and the organization moves on.

A few months later, the same pressure returns because nothing changed about the customer terms or commercial practices that helped create the receivable burden.

Inventory can follow the same cycle. Management sees a large balance and restricts purchasing. Inventory declines and cash improves. Eventually, normal buying resumes, but the forecasting assumptions, product proliferation, purchasing practices, or service expectations that produced the inventory remain unchanged.

The balance starts climbing again.

This does not make the immediate action wrong.

When a business needs cash, it needs cash.

Leadership sometimes has to solve today's problem before it has the luxury of solving anything else.

But once the immediate pressure has eased, the management responsibility becomes larger.

Why did the condition develop?

What changed before the number changed?

That question takes us from financial response into management diagnosis.

## Ask What Changed

One of the most useful questions in business is also one of the simplest:

**What changed?**

When a financial result moves meaningfully, management naturally compares it with a budget, target, prior month, prior quarter, or prior year.

That comparison is important.

But it becomes far more useful when leadership also asks what changed inside the business during the same period.

Suppose gross margin declines materially.

The percentage tells management that the economics of sales have changed.

The next conversation should concern what changed underneath that percentage.

Did supplier prices increase?

Were those increases passed through to customers?

Did discounting become more common?

Did the product mix change?

Did customer mix change?

Did freight become more expensive?

Did production efficiency deteriorate?

Did the company intentionally accept lower margins to enter a new market or win a strategically important account?

Several of those changes could be occurring at the same time.

Some may have been deliberate.

Others may have been unexpected.

Still others may have occurred gradually enough that no one realized their cumulative significance.

The appropriate management response depends heavily on which explanation is true.

The same principle applies when the financial number appears favorable.

Suppose inventory declines significantly.

That could mean management improved forecasting, reduced obsolete stock, shortened lead times, or became more disciplined about purchasing.

Those would generally be positive developments.

But inventory might also have fallen because sales unexpectedly exceeded forecast and the company now lacks enough product to serve customers properly.

The number moved in the same direction.

The operating meaning is completely different.

That is why I have always been cautious about judging business performance through isolated metrics.

Lower is not automatically better.

Higher is not automatically worse.

More inventory may be exactly what a rapidly growing business needs.

Higher operating expenses may reflect an intelligent investment in management capability.

Additional debt may finance equipment that materially improves the economics of the company.

A longer receivable cycle may reflect a deliberate decision to serve larger customers that create substantial strategic value.

The question is not simply whether the number moved.

It is whether leadership understands **why** it moved, what changed in the business, and whether the resulting financial position is consistent with what management intended.

This should not become a complicated methodology.

Owners do not need another process that turns every monthly financial review into an investigation.

The objective is to develop a habit of curiosity.

When something important changes financially, ask what changed in the business first.

Then follow the trail backward.

## Follow the Decision Trail

A financial result can be thought of as the end of a trail.

The number appears on a report today, but the trail may extend backward through several functions and over a period much longer than the reporting month.

Inventory provides a useful illustration.

Suppose inventory increases substantially.

The first step backward may show that Purchasing ordered more product.

Why?

Perhaps the company's sales forecast called for significant growth.

Why did the forecast increase?

Sales may have identified several attractive customer opportunities that management reasonably expected to close.

Those opportunities develop more slowly than expected.

The orders have already been placed.

The inventory remains.

Where did the inventory increase begin?

There may be no single answer.

Purchasing may have ordered according to the forecast it was given. Sales may have had legitimate reasons to believe the opportunities were likely. Management may have wanted enough product available to serve those customers if the growth materialized.

The value of following the trail is not that it inevitably identifies a mistake.

It reveals the chain of assumptions and decisions that produced the financial result.

Receivables can be followed in much the same way.

Finance sees a customer paying in seventy-five days.

The trail may lead back to sixty-day terms negotiated during the original customer relationship. Those terms may have been accepted because the account represented a significant growth opportunity. The customer then routinely pays fifteen days beyond terms because of the way its payment process operates.

What appears today as a collections issue may therefore have begun months earlier as a customer-selection and commercial-terms decision.

Debt may trace backward to an equipment purchase.

The equipment purchase may trace backward to a capacity requirement.

The capacity requirement may trace back to a growth decision.

Operating expenses may trace backward through hiring, compensation, technology, marketing, or infrastructure decisions made over several years.

Cash itself may reflect several trails converging at once.

This is where the concept becomes particularly useful for an owner.

Financial reports show management **where the result appeared**.

Following the decision trail begins to reveal **where management actually has influence**.

Finance can report that inventory increased.

The trail may reveal that the more meaningful management conversation belongs with forecasting, product assortment, order quantities, production runs, or customer requirements.

Finance can report that receivables expanded.

The trail may reveal that the important decision occurred before the invoice existed, when customer terms were negotiated.

Finance can report rising operating expenses.

The underlying commitments may have been made by several different people over the preceding year.

The purpose is not to reconstruct every transaction or assign blame retrospectively.

It is to understand enough of the operating history behind the number that management knows what it is responding to.

That is the bridge from financial visibility to decision visibility.

The report shows the outcome.

The decision trail helps explain the behavior, assumptions, commitments, and circumstances behind it.

And once management begins following those trails, an interesting pattern often emerges.

The decisions it finds are not always careless.

They are not always foolish.

They are not necessarily financially irresponsible.

In many cases, they were perfectly understandable decisions made by capable people trying to accomplish legitimate business objectives with the information available at the time.

That makes the management challenge more complicated.

Because if cash-flow problems were created only by obviously bad decisions, finding the solution would be relatively easy.

The reality is more interesting.

Sometimes good decisions can contribute to bad cash outcomes.

And understanding why requires us to look beyond the quality of any one decision and examine what happens when decisions made throughout the business meet at the enterprise level.

That is where we turn next.

# CHAPTER 3

# When Good Decisions Create Bad Cash Outcomes

## Good People Make Rational Decisions

It would be convenient if cash-flow problems could usually be traced to obviously bad decisions.

Management could identify the mistake, correct the behavior, and move forward. Occasionally, business really is that straightforward. A company buys inventory it clearly does not need, grants credit to a customer it should never have approved, spends money without adequate justification, or makes an investment based on assumptions that should have been challenged.

Those situations happen.

But they are not the situations I find most interesting.

The more difficult management problems arise when capable people make decisions that are entirely rational from where they sit, yet the combined financial result is something no one intended.

Every function in a business has legitimate objectives.

Sales is expected to generate revenue, develop customers, protect important relationships, and create growth.

Purchasing needs reliable supply at attractive economics.

Operations has to produce and deliver what customers expect while balancing efficiency, service, quality, and reliability.

Finance needs financial discipline, visibility, liquidity, and sufficient capacity to meet the company's obligations.

Owners and senior leadership have to think about growth, investment, risk, returns, organizational capability, and the long-term direction of the enterprise.

None of those objectives is inherently wrong.

The difficulty is that they do not always point in the same direction.

Sales may want more product available because customers value immediate delivery. Operations may agree because shortages disrupt production and service. Purchasing may see an opportunity to reduce

unit costs by ordering larger quantities. Finance may be concerned about how much cash is already tied up in inventory.

Everyone can be right from the perspective of the responsibility they are trying to fulfill.

The business still has to live with the combined result.

During my years working across different functions and later with owner-led product businesses, I saw this tension repeatedly. The people involved were rarely trying to create financial problems. They were usually trying to solve the problem directly in front of them.

A salesperson wanted to win an important account.

A purchasing manager wanted to improve cost or secure supply.

An operations leader wanted to prevent stockouts or increase reliability.

An owner wanted to capture an attractive growth opportunity.

The challenge was not necessarily the quality of any one decision.

It was that each decision could create consequences outside the area in which it was made, and those consequences were often less visible to the person making the decision.

This is where cash flow becomes particularly useful as a management lens.

Cash does not care which department made the decision or how reasonable the decision seemed at the time.

Eventually, the financial consequences come together in the same company.

That becomes easier to see when we look at decisions through several different functional perspectives.

## The Sales Decision

Imagine that a salesperson has been pursuing an important prospective customer for several months.

The account could generate meaningful annual revenue, increase the company's credibility in the market, and potentially create additional opportunities. The customer is interested, but reaching an agreement requires several concessions.

The customer wants a lower price than the company normally offers. It wants longer payment terms. It also expects certain products to remain available for rapid shipment.

From the salesperson's perspective, agreeing may be entirely rational.

Large customers often possess negotiating leverage. Companies routinely make pricing and service concessions when the overall relationship justifies them. Maintaining additional inventory for an important account can also make sense if product availability is part of what the customer values.

Sales is doing what management expects Sales to do:

Win worthwhile business.

But the enterprise receives more than the revenue.

A lower price affects the economics of each sale. Longer terms delay the return of cash after the product ships. Additional inventory may require cash before the customer places an order. Increased volume may create requirements elsewhere in the organization.

None of those consequences proves that winning the customer was a poor decision.

The account might still be exceptionally valuable.

The point is that **the sales result is only one part of the enterprise result**.

This distinction becomes increasingly important as a company grows because functional performance is appropriately measured through functional objectives. Sales organizations are expected to increase revenue, win customers, retain accounts, and expand market penetration.

Those measures matter.

The problem begins when the organization assumes that improving a functional measure automatically improves the enterprise.

Sometimes it does.

Sometimes attractive revenue also produces strong margins, reasonable payment timing, efficient inventory requirements, and little need for additional infrastructure.

In that case, the commercial and financial outcomes reinforce each other.

In other situations, the complete relationship is more complicated.

Sales can succeed at the objective it was given while the company simultaneously accepts financial commitments that were not visible in the revenue number alone.

That is not a reason to constrain Sales.

It is a reason to recognize that an enterprise decision includes more than the functional result.

Purchasing and Operations provide another version of the same lesson.

## The Purchasing and Operations Decisions

Purchasing organizations are expected to obtain the materials and products a company needs at competitive costs while maintaining reliable supply.

That responsibility can have an enormous effect on profitability in a product-based business.

Suppose a supplier offers a meaningful reduction in unit cost if the company agrees to purchase substantially more inventory than usual.

From the purchasing perspective, the proposal may be attractive.

The company pays less per unit. It may protect itself against future price increases or supply interruptions. If management expects to use the material eventually, buying ahead could create real economic value.

Purchasing may have done an excellent job.

The enterprise still has to consider another part of the decision:

The additional inventory has to be funded.

That does not make the decision wrong.

If demand is predictable, the product is unlikely to become obsolete, the discount is meaningful, and the company possesses sufficient financial capacity, purchasing ahead may be an excellent use of cash.

The point is simply that lowest unit cost and best enterprise decision are not always identical.

Operations faces similar tradeoffs.

A manager responsible for maintaining high customer service has good reason to dislike stockouts. Additional safety stock can reduce disruption, protect service levels, and make production easier to manage.

That is a legitimate operating objective.

But reducing one form of risk can increase another.

The risk of being out of stock may decline while the amount of cash committed to inventory increases.

Production efficiency creates the same tension. Longer production runs may reduce setup costs and improve utilization. They may also produce more inventory than the company currently needs.

Shorter runs may reduce inventory while increasing production complexity and cost.

Neither answer is universally correct.

Each improves something while potentially placing pressure somewhere else.

That is why management becomes vulnerable whenever a single functional measure becomes the entire definition of success.

Lowest purchase price.

Highest equipment utilization.

Maximum product availability.

Minimum inventory.

Fastest delivery.

Every one sounds desirable in isolation.

The enterprise has to live with the tradeoffs among them.

And ownership itself creates another set of tradeoffs.

## The Owner's Decision

In an owner-led company, it is easy to think of the owner as the person responsible for resolving competing priorities rather than as another source of decisions that create financial consequences.

In reality, some of the most consequential decisions in the business originate with ownership.

Growth is one example.

The owner may decide to enter another market, add a product line, expand geographically, acquire another company, or pursue a substantially higher revenue objective.

The decision may be strategically excellent.

But once made, it can initiate commitments throughout the organization.

People may need to be hired.

Inventory may increase.

Marketing may expand.

Facilities, equipment, systems, or financing may be required.

What began as an ownership decision about direction becomes a series of financial commitments throughout the enterprise.

Capital investment produces another version of the same effect. The owner may approve equipment because it promises better productivity, more capacity, improved quality, or lower operating costs.

Again, the decision may make excellent economic sense.

The company has still chosen to commit resources to that particular use rather than preserving them for another.

Owner distributions create a different but equally legitimate tradeoff.

Owners build businesses partly to create economic value for themselves and their families. Taking distributions from a successful company is not a failure of financial discipline. It is one of the purposes of ownership.

At the same time, cash distributed to owners is no longer available inside the company.

That does not make the distribution wrong.

It means the decision has consequences that have to be considered alongside the needs and objectives of the enterprise.

A financially strong business may be able to support significant distributions while also funding operations, investments, resilience, and growth.

Another company may be profitable yet require most of the cash it generates to support commitments already made.

The same ownership decision can therefore have very different consequences depending on the circumstances of the business.

The larger point is that owners are not outside the decision system.

They are part of it.

Their decisions about growth, investment, financing, people, risk, and distributions create tradeoffs just as functional decisions do.

That is why the owner's perspective has to be broader than the perspective of any single function.

Sales can advocate for customers and growth.

Purchasing can advocate for cost and supply.

Operations can advocate for reliability, productivity, and service.

Finance can advocate for financial discipline.

Ownership and senior leadership have to see how those objectives fit together.

That becomes hardest when every proposal has merit.

The easy leadership decisions are the ones where one alternative is clearly good and another is clearly poor.

Leadership earns its keep when several alternatives are reasonable, resources are limited, and improving one outcome influences another.

That is where the distinction between **functional optimization** and **enterprise optimization** becomes critical.

## Functional Optimization Versus Enterprise Optimization

Every well-run function needs objectives.

Without them, accountability becomes vague.

Sales needs clear expectations around revenue, customer development, retention, and growth.

Purchasing needs measures involving cost, supplier performance, availability, and reliability.

Operations needs objectives for service, productivity, quality, efficiency, and capacity.

Finance needs standards around profitability, liquidity, working capital, financial risk, and control.

None of that is the problem.

The problem arises when success within one function becomes confused with success for the enterprise.

A purchasing manager can reduce unit cost and still make a decision that uses more cash than management intended.

Sales can increase revenue while simultaneously changing pricing, customer terms, inventory requirements, and service commitments in ways that make the overall economics less attractive.

Operations can improve service levels while requiring additional inventory or capacity.

Finance can protect short-term cash so aggressively that the company underinvests in people, equipment, systems, or opportunities capable of creating long-term value.

Even cash flow itself can be optimized too aggressively.

A company could improve short-term liquidity by carrying almost no inventory, refusing customer credit, postponing investment, freezing hiring, reducing marketing, and distributing nothing to owners.

The bank balance might improve.

The business could become weaker.

That is why the goal is not to maximize every function or every Cash Flow Driver independently.

The enterprise has to balance competing objectives.

Sometimes the right decision will intentionally consume cash.

Management may carry more inventory because exceptional availability is fundamental to the company's competitive position.

It may accept longer payment terms because a strategically important customer creates enough value to justify them.

It may hire ahead of growth because the organization needs capability before demand arrives.

It may increase debt because an investment opportunity deserves to be pursued before internally generated cash is available.

Those decisions can reduce near-term financial capacity while still strengthening the business over time.

The critical distinction is whether management understands the tradeoff before making the commitment.

That is what enterprise thinking adds.

It does not tell Sales to stop selling.

It does not tell Purchasing to stop pursuing lower costs.

It does not tell Operations to stop protecting customers.

And it does not give Finance veto power over every significant business decision.

The objective is not centralized micromanagement.

As companies grow, decision-making has to become more distributed, not less.

What leadership must provide is a way of thinking that encourages managers to look beyond the measure directly in front of them and consider what their decisions require from the business as a whole.

Cash flow can help expose those consequences because it provides a common economic lens.

A decision may increase revenue.

Reduce cost.

Improve service.

Create capacity.

Lower risk.

Increase owner returns.

Each of those outcomes may be worthwhile.

Management can still ask what the decision requires financially, when those resources will be committed, when the expected benefits are likely to appear, and what other parts of the business may be affected in the meantime.

Those questions do not guarantee the correct answer.

Sometimes there may not even be one clearly correct answer.

They make the decision more complete.

Over the years, I have seen businesses encounter financial pressure not because management was careless, but because capable people were doing reasonably good jobs pursuing the objectives directly in front of them.

Sales pursued revenue.

Purchasing pursued cost.

Operations pursued reliability.

Management pursued growth.

Ownership pursued investment and returns.

The difficulty appeared in the space between those objectives, where no single function had complete visibility into the combined result.

That space belongs to leadership.

And once leadership understands the distinction between functional optimization and enterprise optimization, we are ready to look more closely at the specific decision families behind the ten primary Cash Flow Drivers.

We begin where many owner-led businesses naturally begin:

With growth, customers, pricing, and the terms under which the company chooses to generate revenue.

# CHAPTER 4

# Growth and Revenue Decisions

## Growth Is a Decision Before It Is a Result

Growth occupies a special place in business.

Owners pursue it. Employees often associate it with opportunity. Lenders and investors may view it as evidence of momentum, and strategic plans routinely organize priorities around achieving it. When revenue rises, the natural assumption is that the company is moving in the right direction.

In many cases, that assumption is entirely justified.

Growth can strengthen market position, create economies of scale, provide opportunities for employees, increase profitability, and contribute to substantial enterprise value.

But reported growth is a result.

Long before the additional revenue appears on an income statement, management has usually made a series of decisions intended to create it.

Which markets should we pursue?

Which products should we emphasize?

Which customers do we want?

What level of growth are we trying to achieve?

How quickly do we want to pursue it?

What commitments will the business have to make if the opportunity develops as expected?

For a product-based company, those questions matter because growth typically requires resources before all of the resulting cash arrives.

Products have to be manufactured or purchased. Inventory may need to be positioned before orders are received. Sales and marketing resources may be added. Operations may need additional people or capacity. Once the product ships, customers may not pay for another thirty, sixty, or ninety days.

The company can therefore commit financial resources to growth well before the cash associated with that growth returns to the business.

That is why I think of growth as a decision before I think of it as a number.

By the time management sees a 15 percent or 25 percent increase in revenue on the financial statements, many of the decisions required to produce that increase have already occurred.

Some growth is highly intentional. Management selects a market, develops a plan, commits resources, and pursues the opportunity deliberately.

Other growth arrives more opportunistically. An unexpected customer appears. An existing account expands rapidly. A new product performs better than expected. A competitor exits a market and demand shifts.

Both forms can create substantial value.

Both can also require resources.

During my years working with product-based SMBs, I encountered owners who were surprised that strong growth had not produced the improvement in cash they expected. The company was selling more, often earning more, and sometimes reporting record results, yet the owner felt as though the business had less financial breathing room rather than more.

There was not necessarily anything wrong with the growth.

The apparent contradiction usually became easier to understand once management looked at what the additional revenue required before the associated cash arrived.

More business had required more resources.

That is not an argument against growth. Well-managed growth is one of the primary ways businesses create value.

It is an argument for seeing growth as a complete management decision rather than simply a sales objective.

The company is not deciding only how much revenue it wants.

It is also deciding what kind of revenue it wants to create.

And those two questions are not the same.

## Not All Revenue Is Created Equal

Imagine two customers that each generate $1 million of annual revenue.

On a sales report, they look identical.

Economically, they may be very different relationships.

The first customer buys standard products already carried by the company. It pays the established price, accepts normal freight arrangements, requires little unusual service, and pays according to standard terms. Existing people, systems, inventory, and capacity can comfortably support the account.

The second customer generates the same $1 million but negotiates lower pricing, expects longer payment terms, requires dedicated inventory, asks for customized packaging, frequently needs expedited shipments, and creates additional administrative and service requirements.

Both customers generate $1 million of revenue.

They do not necessarily generate the same margin.

They do not require the same inventory.

They do not create the same receivable.

They do not consume the same operating capacity.

And they do not necessarily create the same amount of financial value for the enterprise.

This is what I mean by **revenue quality**.

The business does not receive revenue in isolation. It receives the complete economics attached to that revenue.

Those economics include price and margin, but they can also include product mix, inventory requirements, payment timing, freight, service demands, customization, capacity requirements, and the amount of management attention necessary to support the relationship.

Two customers that look almost identical at the top of the income statement can therefore have considerably different effects on the rest of the business.

Customer mix can change these characteristics gradually.

A company may move from serving many smaller customers toward fewer large national accounts. Strategically, that may be exactly what management intends. The larger accounts can provide scale, credibility, predictable volume, and access to markets that would otherwise be difficult to reach.

They may also possess substantially more negotiating leverage.

Pricing may become tighter. Terms may lengthen. Service expectations may rise. Inventory commitments may increase.

The business may become larger and strategically stronger while simultaneously requiring more financial capacity to support each dollar of revenue.

There is no contradiction in that.

It simply means revenue growth has an economic structure underneath it.

Product mix creates similar differences. One product may generate an attractive margin but require substantial inventory and long lead times. Another may produce a somewhat lower margin but move rapidly through the business. A third may be strategically valuable because it opens the door to other products or customers.

There is no universal rule that one type of revenue is superior to another.

The management responsibility is to understand what the revenue requires and what the company receives in return.

One of the first decisions influencing that relationship is the price.

## Pricing Is a Cash Flow Decision

Pricing is normally discussed in terms of competitiveness, customer value, revenue, and margin.

Those are exactly the right considerations.

But pricing also affects cash-generation potential because the amount the company ultimately receives from a sale begins with the price management agrees to charge.

That may seem obvious, yet pricing decisions often occur far from any explicit cash-flow discussion.

A salesperson offers a discount to close an order. Management delays an increase because competitors have not moved. A major customer negotiates special pricing in exchange for anticipated volume. A promotion is introduced to gain market share or move inventory.

Each decision may make sense.

The financial importance emerges when those decisions accumulate across a meaningful revenue base.

Consider a company generating $15 million in annual sales. A one-percent difference in realized pricing represents $150,000 of revenue before considering any corresponding change in volume or cost.

That simple arithmetic is not a pricing strategy.

The more important management point is that pricing often changes incrementally rather than through one dramatic decision.

List prices.

Discounts.

Customer-specific agreements.

Promotions.

Exceptions.

Negotiations.

Delayed increases.

Each affects how much economic value the company retains from what it sells.

But the answer is not simply to raise prices.

A lower price may generate enough additional volume to produce a superior enterprise result. A strategic discount may help the company enter an important account. An increase that looks attractive mathematically may reduce volume, damage a valuable customer relationship, or create an opening for a competitor.

The purpose here is not to teach pricing strategy.

It is to recognize that a pricing decision has consequences beyond the transaction in which it is made.

The price affects the margin available from the sale. If pricing changes volume, the company may also require different amounts of inventory, receivables, labor, or capacity to support that volume.

Pricing therefore illustrates the principle we established in Chapter 3.

Sales may legitimately focus on what is required to win the business.

Finance may focus on margin and cash generation.

Operations may focus on whether the company can support the expected volume.

The enterprise needs to understand all of those perspectives.

Pricing becomes especially important when costs are changing. If supplier costs, wages, freight, insurance, or other inputs rise while customer prices remain unchanged, the company absorbs the difference.

Management may have good strategic reasons for doing that temporarily.

Choosing not to change a price is still a pricing decision.

Discounts deserve the same perspective. A discount is not automatically a mistake. Sometimes giving up part of the economics of a transaction creates something more valuable in return—volume, access, customer loyalty, a strategic relationship, or entry into a market.

The important question is whether management understands the exchange it is making.

That requires looking beyond the sale itself and considering the customer relationship as a whole.

## The Customer Decision

One of the most consequential commercial decisions a product business makes is deciding **which customers it wants to serve and under what conditions**.

Yet customer acquisition is frequently viewed primarily as a Sales responsibility.

Sales identifies the opportunity, develops the relationship, negotiates the terms, wins the account, and moves to the next opportunity.

The customer does not remain inside Sales after the agreement is signed.

The relationship enters the entire business.

Purchasing may need additional materials or finished goods. Operations may need different production schedules. Warehouse employees may handle special packaging or shipping requirements. Customer service may absorb new reporting or administrative demands. Finance carries the receivable. Management may eventually add people, equipment, technology, or capacity.

What began as a sales opportunity becomes an enterprise relationship.

Large customers make this particularly visible.

A significant account can transform a smaller company. The customer may provide substantial volume, credibility, purchasing leverage, production efficiencies, and access to opportunities that would have been difficult to obtain otherwise.

That value can be enormous.

Large customers can also have considerable bargaining power.

They may expect lower prices, longer terms, guaranteed inventory availability, specific technology or compliance requirements, special packaging, dedicated support, or penalties when service expectations are not met.

None of those requirements automatically makes the customer unattractive.

The issue is whether the complete relationship creates sufficient value to justify what the business is committing to support it.

There is another dimension that becomes increasingly important as a customer grows:

**concentration.**

A customer that represents 2 percent of revenue creates a different strategic relationship from one representing 20 or 30 percent.

A large customer can be extraordinarily profitable and worth serving. But as the relationship becomes more significant, the company's dependence on that customer's decisions can also increase.

A change in volume, pricing demands, payment practices, sourcing strategy, or supplier relationships may have consequences throughout the business.

Again, concentration does not make the customer bad.

It changes the nature of the decision.

Management has to understand not simply how much revenue the account creates but how much of the company's economics, financial capacity, operating structure, and future expectations have become connected to it.

This is why **winning business** and **creating financially attractive business** are related but not identical.

Over the years, I have seen owners become understandably excited about the size of a new account and initially focus on the revenue opportunity. As the relationship developed, the company discovered what else came with it: additional inventory, operating requirements, customer-service activity, receivables, and perhaps new people or capacity.

The company had not simply won revenue.

It had made commitments.

That is why one of the most useful questions management can ask about a significant customer opportunity is not merely:

**How much can we sell?**

It is:

**What does serving this customer require from the business?**

The answer may confirm that the account is an outstanding opportunity.

It may reveal economics management had not initially considered.

Either way, leadership has a more complete understanding of the decision before the commitments become embedded in the organization.

One of the most important of those commitments is often established during the original customer negotiation.

How long will the company wait to be paid?

## The Terms Decision

Accounts receivable is naturally associated with Finance.

Finance monitors aging, evaluates credit exposure, follows up on overdue invoices, and helps management understand how quickly customers are paying.

Those responsibilities are important.

But one of the most consequential decisions affecting a receivable may have occurred before the invoice even existed.

It occurred when the company agreed to the customer's payment terms.

Suppose two customers buy identical products at identical prices and generate identical annual revenue. One has thirty-day terms and the other sixty-day terms.

From a revenue perspective, they may appear essentially the same.

From a cash-timing perspective, they are not.

The company serving the sixty-day customer has agreed to leave its financial resources committed to the transaction for another thirty days. The business still has payroll, supplier obligations, operating expenses, and other commitments during that period.

That additional time has to be funded somehow.

It may be funded from cash generated elsewhere in the company, supplier credit, borrowing, owner capital, or some combination of them.

Longer terms may be entirely appropriate.

Some industries operate that way. Large customers may require them. An economically attractive account can easily justify the additional working-capital commitment.

The point is not that thirty-day terms are good and sixty-day terms are bad.

The point is that terms are part of the economic proposition.

This distinction becomes especially important when exceptions accumulate.

A company may believe it has a standard thirty-day policy while Sales routinely agrees to forty-five or sixty days when circumstances justify an exception.

Each decision may make sense.

Over time, however, the actual financial characteristics of the customer base may become quite different from the stated policy.

By the time Finance begins collecting the resulting receivables, much of the original cash-flow consequence has already been established.

A customer paying on the sixtieth day under agreed sixty-day terms is not late.

The company made a commercial decision to finance that customer for sixty days.

That is why receivables belong in more than one management conversation.

Later, we will look at receivables as part of working capital and the operating cash cycle.

Here, the important point is where the receivable begins:

**with a customer decision.**

Customer selection, pricing, payment terms, volume, and service expectations collectively establish much of the financial architecture of the revenue before the first invoice is issued.

And as revenue grows, the cumulative financial requirement can become substantial.

## Growth Has to Be Funded

One of the persistent assumptions about growth is that a profitable company should automatically generate more cash as sales increase.

Over a sufficiently long period, profitable growth should create economic value.

But the timing of profit and cash can be very different, particularly in a product-based business.

Imagine a company entering a period of rapid growth.

Orders are increasing. The sales pipeline is strong. Management believes the opportunity is real.

To support that demand, the company begins committing resources.

Inventory increases before some of the sales occur. People may be added. Operating requirements expand. Once products ship, revenue and profit may be recorded even though the customer has not yet paid.

Then the next layer of growth begins while the company is still waiting for cash from the previous one.

This can produce a condition that seems contradictory on the surface:

The business is growing.

It is profitable.

And cash is becoming tighter.

Years ago, I began using the phrase **Growing Broke** to describe that situation because it captures what many owners experience. The company appears increasingly successful by conventional measures, yet each additional layer of success seems to require more cash.

There is nothing inherently dysfunctional about that.

Growth frequently needs financing.

The problem is not that growth consumes cash before generating it.

The problem is when management treats that requirement as an unexpected side effect rather than part of the growth decision itself.

A company deciding to pursue substantial growth is therefore making more than a revenue decision.

It is also deciding to support the financial commitments attached to that growth.

The exact requirements will depend on the business, the products, the customers, the payment terms, the margins, and the pace at which growth occurs.

This is not the place for formulas or growth calculations.

The management principle is enough:

**Growth has to be funded.**

That means leadership should understand the financial architecture of the opportunity before the company is fully committed to it.

What kind of customers are driving the growth?

What pricing accompanies the revenue?

What payment terms will the company accept?

What resources will have to be committed before the resulting cash returns?

Those questions do not make management less ambitious.

They make the growth decision more complete.

A company can deliberately decide that an opportunity deserves a significant commitment of financial resources because management believes the expected long-term value justifies it.

That may be exactly the right decision.

What leadership wants to avoid is discovering the financial requirement only after the growth has already dictated the commitments.

That is the central lesson of this chapter.

**Revenue is not financially neutral.**

The amount of revenue matters.

So does the kind of revenue.

The price at which it is generated matters.

The customers behind it matter.

The terms attached to it matter.

And the resources required to support it matter.

Growth, Pricing, and Receivables may appear as separate Cash Flow Drivers when management looks at a financial report.

Commercially, they begin much closer together.

They begin with decisions about how the company chooses to create revenue.

Once those decisions have been made, the next question is what it costs the business to produce, deliver, and support that revenue.

That takes us from the customer side of the equation to the decisions embedded in margin and operations.

# CHAPTER 5

# Margin and Operating Decisions

## COGS Begins With Business Decisions

Chapter 4 focused on the decisions that shape revenue—growth, pricing, customers, and the terms under which the company chooses to do business.

But generating revenue is only one side of the economic equation.

The company also has to decide how it will produce, deliver, and support that revenue. Those decisions eventually become visible in margin and operating expenses.

When owners review an income statement, cost of goods sold usually appears as a financial category between revenue and gross profit. In a product-based business, it may include materials, purchased products, direct labor, freight, manufacturing costs, or other expenses directly associated with producing and delivering what the company sells.

Management watches that number closely because relatively small changes in COGS can have a meaningful effect on gross margin and, ultimately, on the amount of cash the business has the potential to generate.

What the income statement cannot show by itself is how many decisions occurred before those costs appeared there.

A manufacturer chooses suppliers, materials, production methods, staffing levels, run sizes, quality standards, freight arrangements, and service requirements. A distributor makes decisions about sourcing, supplier relationships, purchasing practices, product assortment, logistics, and how inventory moves through the business.

Management also determines how much complexity the business is willing to support, what level of quality customers expect, how quickly orders should be fulfilled, and what tradeoffs the organization is prepared to make among cost, reliability, responsiveness, and service.

Those are operating decisions first.

Eventually, many of their economic consequences become visible in COGS and gross margin.

COGS is therefore another place where the management result we discussed in Chapter 1 becomes visible. Accounting can tell leadership what the company spent. Understanding why the company spent that amount requires looking at the operating and commercial decisions behind it.

Supplier selection provides a straightforward example.

One supplier may offer the lowest price. Another may charge more but provide shorter lead times. A third may be more expensive while delivering exceptional quality and reliability.

The invoice captures the purchase price, but the enterprise experiences considerably more than the invoice.

A lower-priced supplier with long lead times may require the business to carry more inventory. A supplier with inconsistent quality may create scrap, rework, returns, production interruptions, or customer-service problems. A more expensive supplier with exceptional reliability may allow the business to operate with less inventory and fewer disruptions.

None of those alternatives is automatically superior. The right decision depends on the complete economics of the relationship and what the business is trying to accomplish.

Production decisions create similar tradeoffs.

Longer production runs may reduce changeover time and improve labor or equipment efficiency, but they may also create more finished-goods inventory than the company needs immediately. Shorter runs can reduce inventory while increasing setup time, complexity, and production cost.

Neither approach is universally correct because each improves one aspect of performance while potentially creating consequences somewhere else.

Product and customer mix can affect COGS in equally important ways. Two products sold at similar prices may require very different amounts of labor, material, machine time, packaging, freight, and quality control. A large customer may improve production efficiency through volume while simultaneously requiring special packaging, service, freight, or compliance activities that increase costs elsewhere in the organization.

Eventually, the financial statements consolidate all of those decisions into numbers.

Management's responsibility is to look behind those numbers and understand whether the economics developing inside the business are consistent with what leadership intended.

That becomes particularly important because the lowest visible cost does not always produce the lowest economic cost for the enterprise.

## Lowest Cost Is Not Always Lowest Economic Cost

Cost reduction is attractive for an obvious reason.

If a company can buy the same material for less, produce the same product using fewer resources, or obtain a meaningful volume discount, the improvement may flow directly into margin. In many circumstances, that is exactly what good management should pursue.

Disciplined purchasing and operating efficiency are fundamental to a strong product-based business.

The complication arises when a decision that reduces one visible cost creates another financial or operating commitment somewhere else.

Suppose a supplier offers a substantial discount if the company purchases significantly more than its normal quantity. Purchasing can calculate the savings precisely, and the reduction in unit cost may be meaningful.

If demand is predictable, the material will be used quickly, and the company has adequate financial capacity, the larger order may be an excellent decision.

But suppose the material remains in inventory for nine months.

The company has now committed cash for nine months in order to obtain the lower purchase price. There may also be additional storage requirements, greater exposure to obsolescence or damage, and less flexibility to use that same cash somewhere else.

The discount has not disappeared, and the company may still have made the correct decision.

The point is that purchase price alone does not describe the complete economics.

Sourcing decisions can create the same tension. A company may move to a lower-cost supplier located much farther away. Unit economics improve, but lead times increase. To protect against delays or interruptions, management may carry more inventory. Minimum order quantities may rise, freight may become more complicated, and the organization may become less responsive when demand changes unexpectedly.

Again, the lower-cost supplier may still be the best alternative.

Or a higher-cost supplier may create the better enterprise result because of reliability, speed, quality, or reduced inventory requirements.

Quality provides another example. A supplier offering the lowest quoted price may create additional scrap, rework, warranty claims, returns, or production disruptions. Paying more for higher quality can sometimes lower total economic cost even though the invoice itself is higher.

This is where the distinction between functional and enterprise optimization that we discussed in Chapter 3 becomes practical.

Purchasing is appropriately focused on cost. Operations is appropriately concerned with reliability and efficiency. Sales values responsiveness to customers. Finance cares about margin and financial capacity.

Leadership has to understand what happens when those objectives interact.

That does not mean the business should automatically choose the more expensive alternative in the name of total value. Sometimes the lowest-cost supplier truly is the best supplier.

The management responsibility is to understand the tradeoff rather than assume that improving one cost measure automatically improves the enterprise.

That same logic becomes even more important when we move beyond the direct costs of the product and look at the operating structure that supports the business.

## Operating Expenses Are Commitments

Operating expenses often receive intense attention when cash becomes tight.

Payroll, marketing, technology, facilities, insurance, professional services, travel, administrative costs, and dozens of other expenses compete for the cash the company generates. When leadership needs to improve profitability or conserve cash, reducing operating expenses may therefore seem like an obvious place to begin.

But operating expenses deserve attention long before management decides whether something should be reduced or eliminated.

They deserve attention when the original commitment is made.

A company rarely wakes up one morning and discovers that annual operating expenses suddenly increased by $1 million. More often, the cost structure develops through a series of individually understandable decisions.

Management hires several people. Marketing expands. New technology is added. Compensation increases. Additional space is leased. Employee benefits improve. Outside expertise is engaged. Infrastructure is built to support a larger organization.

Each decision may have a legitimate purpose.

Over time, however, those individual decisions become the operating structure of the company.

That distinction matters because many operating expenses are not easily reversed without consequences. Hiring an employee creates a different commitment from purchasing office supplies. A lease establishes an obligation extending into the future. Technology platforms become embedded in processes. Compensation decisions influence employee expectations. Marketing programs may require time before their effectiveness can be judged fairly.

Once an organization is built around a particular level of activity, shrinking that structure can also be difficult and disruptive.

For that reason, I prefer to think of many operating-expense decisions as commitments rather than simply expenditures.

The amount leaving the bank account this month is only part of the decision. Management may also be committing future cash, organizational capacity, leadership attention, and operating resources for months or years.

This becomes particularly important during periods of expected growth.

Companies frequently need to build capability before the additional revenue arrives. A business may need another manager before the organization becomes overwhelmed. Salespeople may need to be hired before they can create a meaningful pipeline. A technology platform may need to be implemented before transaction volume exceeds existing systems. Additional space may have to be secured before every square foot is fully utilized.

Those decisions can be excellent investments in the future of the company.

The timing, however, creates a financial gap between when the business begins paying for the capability and when the expected benefit fully develops.

If growth arrives as expected, the investment may look prescient. If growth develops more slowly than management anticipated, the same cost structure can create pressure on profit and cash.

The original decision may still have been reasonable based on the information available at the time. What changed may be the assumption that supported it.

This is why understanding operating expenses requires more than asking whether the company is spending too much. Leadership also needs to understand what commitments it has made, what those commitments were intended to accomplish, and whether the assumptions supporting them remain valid.

Few operating commitments make that point more clearly than decisions involving people.

## People Decisions Have Long Tails

Hiring is one of the most important investments an owner-led business makes because the right people create capabilities the owner and existing management team cannot build alone.

Employees develop customers, improve operations, manage complexity, solve problems, create products, strengthen systems, and ultimately allow the organization to become more capable. Evaluating a hiring decision solely as an expense therefore misses much of its economic significance.

At the same time, evaluating the decision solely on the basis of salary understates the financial commitment the business is actually making.

An employee earning $80,000 does not represent only an $80,000 decision.

Payroll taxes and benefits add to the direct cost. The person may need a computer, software, workspace, training, travel, equipment, or administrative support. A salesperson may require marketing resources and customer support. A manager may eventually need additional people.

As the organization expands, further investments in HR, IT, Finance, and management infrastructure may follow.

There is also a timing difference between the commitment and the expected return. The company begins carrying the cost immediately, while the full economic benefit may take considerably longer to develop.

A salesperson may need months to build a pipeline. A manager may spend substantial time learning the business before stronger leadership begins producing visible results. A technical employee may be hired ahead of a product launch or expansion that has not yet occurred.

None of this argues for delaying necessary hiring.

Companies can damage themselves by waiting too long just as surely as they can by hiring too early. An owner who refuses to build management capability can become the bottleneck limiting the organization. An understaffed operation can create overtime, burnout, turnover, customer-service problems, or quality issues that eventually cost far more than the additional payroll would have.

The point is that hiring creates both capability and commitment.

Owners often see this particularly clearly after a period of rapid expansion. During growth, each new hire may feel essential because the organization is stretched and opportunities are plentiful.

If revenue later flattens or grows more slowly than expected, the company suddenly sees how much of its cost structure was built around assumptions about the future.

That does not automatically mean the hiring decisions were wrong. It means their economics depended partly on what management expected to happen next.

The same principle applies across operating expenses.

Marketing spending assumes some form of future return. Technology investments are intended to improve capability, efficiency, control, or scalability. Facilities are acquired because management expects to need the space. Professional services are engaged because the company expects specialized expertise to create value.

Good management does not avoid those commitments.

It makes them deliberately and continues evaluating whether the assumptions behind them remain valid.

That is very different from treating financial discipline as a synonym for cutting expenses.

## Cost Discipline Is Not Cost Cutting

When business conditions become difficult or cash tightens, expense reductions may be necessary.

Some spending should be stopped. Certain projects should be postponed. Costs that accumulated without producing sufficient value may deserve to be eliminated.

Every business should periodically challenge whether the resources it is committing continue to make sense.

The danger is allowing a short-term need to conserve cash to evolve into a broader philosophy that less spending is always better. A business can reduce expenses while weakening itself.

Preventive maintenance can be postponed long enough that equipment reliability deteriorates. Positions can remain unfilled until good employees become overloaded. Marketing can be reduced so aggressively that the sales pipeline suffers months later. Technology investments can be delayed until manual processes and workarounds consume increasing amounts of employee time.

Training, quality initiatives, and management development can also be reduced with consequences that do not become visible until much later.

The relevant issue is not that these expenditures deserve automatic protection.

It is that management should understand what it is receiving in exchange for the resources being committed before deciding that eliminating the cost creates value.

That is the distinction I make between cost cutting and cost discipline.

Cost cutting focuses primarily on reducing the amount being spent. Cost discipline asks whether the resources being used are producing enough value to justify their continued commitment.

Some costs are necessary simply to operate. Others protect the company against risk. Some create capability, support customers, or enable growth. Still others remain in the business because nobody has questioned them in years.

They may all appear as expenses on the same financial statement, but economically they are not identical.

The same reasoning applies to gross margin. Management should certainly understand and challenge the costs required to manufacture or acquire the products the company sells. But minimizing every component of cost can undermine quality, reliability, responsiveness, or the customer proposition that allows the business to earn an attractive price in the first place.

The objective is not the lowest possible cost structure.

It is an operating model that uses resources intelligently and supports the economics, strategy, and financial strength of the enterprise.

That brings us back to the central argument of this guide.

Cost of Goods Sold and Operating Expenses do not simply happen to a business. They emerge from choices involving suppliers, materials, production, freight, people, facilities, technology, service levels, quality, product complexity, and organizational capability.

Some of those choices are made deliberately at the executive level. Others develop gradually through everyday operating decisions. Eventually, the financial statements reveal what those choices collectively produced through gross margin, operating expenses, profit, and cash generation.

But the financial numbers arrive after the operating choices.

Chapter 4 examined the decisions that determine what kind of revenue the company chooses to create and under what commercial conditions. This chapter has focused on what the business chooses to spend in order to produce, deliver, and support that revenue.

The next chapter moves into a different kind of commitment.

Some of the largest uses of cash in a product-based business do not immediately appear as expenses at all. Instead, they remain inside the operating cycle as inventory and receivables, offset in part by the credit suppliers provide through accounts payable.

That is working capital, and it provides perhaps the clearest example yet of how decisions throughout the business become cash-flow consequences.

# CHAPTER 6

# Working Capital Decisions

## Working Capital Is Where Decisions Accumulate

Chapter 5 focused on the decisions that determine much of what a company spends to produce, deliver, and support its revenue.

But in a product-based business, some of the largest commitments of cash do not immediately appear as expenses on the income statement.

They remain inside the operating cycle.

For many owners, working capital is where the difference between profitability and financial flexibility becomes most visible. A company can have strong sales, attractive margins, and a profitable income statement while still feeling as though cash is perpetually scarce.

When that happens, a significant part of the explanation may be sitting in inventory and receivables, offset to some degree by the credit suppliers provide through accounts payable.

Working capital is appropriately discussed in financial terms. Finance needs to understand how much money is committed to the operating cycle, how those requirements are changing, and what the company may need to finance as it grows.

But describing working capital primarily as a financial concept can obscure where much of it actually comes from.

Inventory begins with decisions about what to buy or produce, how much to carry, how quickly customers expect delivery, which products the company wants to offer, how suppliers operate, and how much uncertainty management wants to protect against.

Receivables begin earlier than the collection process. As we saw in Chapter 4, customer selection, credit decisions, pricing negotiations, payment terms, and commercial exceptions can determine how long the company expects to wait for its money before the first invoice is ever issued.

Accounts payable also begins before Finance schedules a payment. Supplier selection, purchasing volume, negotiated terms, order quantities, and supplier relationships all influence how long the business has before cash must leave the company.

These decisions do not necessarily occur at the same time or involve the same people.

Purchasing may commit cash to inventory weeks or months before the product is sold. Operations may determine how much product needs to be available without knowing precisely when customers

will ultimately pay. Sales may negotiate customer terms independently of the supplier terms under which the company acquired the product.

Eventually, the financial system brings all of those consequences together. Inventory appears on the balance sheet. Customer invoices become receivables. Supplier invoices become payables.

By then, many of the decisions determining how much cash the operating cycle requires have already been made.

This is why working capital can expand substantially without anyone consciously deciding to invest another $500,000 or $1 million in it. The company does not necessarily approve a single expenditure called "working capital." It makes hundreds of commercial and operating decisions that collectively determine how much working capital the business requires.

Growth can amplify the effect.

As sales increase, more product may need to move through inventory, more money may be owed by customers, and more purchases may be made from suppliers. If inventory turns more slowly, customer terms lengthen, or supplier terms shorten at the same time, the cash requirement can grow even faster than revenue.

That does not mean the business is doing something wrong.

It means part of the financial requirement of operating and growing the company is accumulating inside the working-capital cycle.

For a product-based business, nowhere is that more tangible than inventory.

## Inventory Is a Decision, Not Just an Asset

Inventory occupies an unusual position in the mind of an owner.

It is an asset because the company expects to sell it or use it to produce something that will be sold. At the same time, it represents cash that has been committed to a particular purpose and cannot be used somewhere else while the inventory remains in the business.

Both descriptions are true.

That dual nature matters because conversations about inventory can easily become oversimplified. When cash is tight, inventory is sometimes treated as though it is inherently undesirable. When customer service or supply reliability is under pressure, carrying more inventory can appear to be the obvious answer.

Neither perspective captures the complete management challenge.

Product businesses hold inventory for legitimate reasons. Customers may expect immediate availability. Suppliers may have long lead times. Production schedules may require raw materials to be

available before manufacturing begins. Seasonal demand may force the company to build inventory well ahead of sales.

Minimum order quantities can make smaller purchases uneconomical, while uncertainty in the supply chain may justify additional protection against disruption.

Inventory can therefore create real economic value. It helps the company serve customers, keep production operating, respond to demand, and protect itself against uncertainty.

The relevant management question is not simply whether inventory is high or low.

It is whether the amount and type of inventory the company carries are consistent with the decisions management has made about customers, products, suppliers, service levels, production, risk, and growth.

Consider a distributor that promises rapid delivery across a broad product line. That customer proposition may require substantially more inventory than a competitor that carries fewer products or accepts longer delivery times.

The additional inventory is not necessarily evidence of poor management.

It may be part of the company's strategy.

A manufacturer with long supplier lead times faces a similar issue. Carrying additional raw materials may protect production from interruptions that could otherwise be extremely costly. A seasonal company may deliberately build inventory months before its strongest selling period because the product has to be available when customers are ready to buy.

In each case, inventory is doing something for the business.

But it still has to be funded.

That is the tradeoff management needs to see clearly. Inventory can create value and consume financial capacity at the same time.

Once we recognize that dual role, the more useful question becomes how all of that inventory got there in the first place.

## The Decisions That Build Inventory

A significant increase in inventory rarely results from one decision.

More often, inventory grows through a series of decisions that make sense individually.

The sales forecast increases, so Purchasing orders more product.

Operations raises safety stock because shortages have disrupted production or customer service.

A supplier offers better pricing at a larger order quantity.

Production increases run sizes to reduce changeovers and improve efficiency.

Management adds products because customers want greater selection.

A large customer requires dedicated inventory.

A new product launches successfully—or more slowly than expected.

Older products continue to sell, but not quickly enough to disappear as new products are added.

Each decision can have a legitimate rationale.

The financial consequence appears when they accumulate.

Imagine a company with hundreds or thousands of SKUs. Management does not need to make a dramatic decision to increase inventory by $500,000. A relatively small increase across enough products can produce the same result.

That is one reason inventory can grow almost invisibly.

No individual decision seems especially consequential, but the balance sheet eventually reveals the cumulative effect.

Forecasting plays an important role because inventory decisions frequently depend on expectations about what will happen next. If management expects sales to increase, buying or producing ahead of that demand may be completely rational.

The difficulty is that forecasts are estimates, not promises.

When expected sales arrive later than anticipated, the inventory has already been purchased or produced. The decision may have been reasonable based on the information available at the time, but the cash remains committed longer than management expected.

New products can create a similar pattern. Adding a product may require initial inventory before management knows exactly how demand will develop. If the product succeeds, that investment supports growth. If it moves slowly, the cash remains committed while the business determines what to do next.

Product proliferation can magnify the issue over time.

One new SKU rarely changes the financial position of a business. Dozens or hundreds of additions can. If older products are not removed at roughly the same pace, the breadth of the assortment expands and inventory can grow even without a deliberate decision to increase total stock.

Customer commitments add another layer. Sales may promise availability because rapid delivery is important to winning or retaining an account. The inventory supporting that promise may be economically justified, but it is still part of the financial commitment embedded in the customer relationship.

Purchasing economics can push in the same direction. Larger orders may reduce unit costs or freight expense. As we discussed in Chapter 5, those savings may be real while the additional inventory simultaneously requires more cash.

This is why simply telling a product business to "reduce inventory" is not particularly useful.

Inventory exists for reasons.

The management responsibility is to understand those reasons and determine whether the financial commitment remains consistent with the value the inventory is intended to create.

Sometimes the answer will be to carry less.

Sometimes carrying more will be the better decision.

The important point for our discussion is that the cash consequence belongs in the decision from the beginning.

If leadership wants to understand why inventory changed, it has to follow the trail into Purchasing, Sales, Production, Operations, forecasting, product strategy, supplier relationships, and customer commitments.

By the time Finance sees excess inventory, some of the decisions that created it may be months or even years old.

Receivables tell a similar story, but the decision trail often begins with the customer before the sale ever occurs.

## Receivables Begin Before the Invoice

Accounts receivable is frequently treated as a collections issue.

When balances increase or customers pay more slowly, Finance reviews the aging, contacts overdue accounts, resolves disputes, and works to convert receivables into cash. Those activities are necessary, and disciplined collections are an important part of financial management.

But focusing exclusively on collections begins too late to explain the entire receivables story.

We established in Chapter 4 that a receivable begins economically when the company decides to sell to a customer on credit and agrees to the conditions under which payment will be made. The invoice formalizes the obligation, but many of the factors determining how long the company's financial resources will remain committed were established during the commercial relationship.

Here, that commercial decision becomes part of a larger working-capital cycle.

The company may have purchased or manufactured inventory before making the sale. Once the product ships, the inventory leaves the balance sheet, but the cash may not return immediately. Instead, part of the company's financial investment moves into accounts receivable while the business waits for the customer to pay.

How long it remains there depends partly on the decisions made before the sale.

Customer selection matters. A smaller local customer may pay in thirty days while a national account expects sixty or ninety. The national account may provide substantial revenue, excellent credit quality, and important strategic value while still requiring the company to finance the transaction for a much longer period.

Terms matter as well.

If the company agrees to sixty-day terms, a customer paying on day sixty is doing exactly what was negotiated. Finance cannot reasonably solve that cash requirement by becoming more aggressive about collections.

The business made a commercial decision to wait sixty days for its money.

Exceptions can gradually reshape the receivables profile in much the same way that individual inventory decisions can reshape the inventory balance.

A company's standard terms may remain thirty days on paper while important customers receive forty-five, sixty, or ninety days through individual negotiations. Sales may have good reasons for each exception, particularly when competing for larger accounts.

Over time, however, the actual economics of the customer base can become considerably different from what the stated policy suggests.

Not every receivable delay begins with terms.

Operational execution can also affect how quickly revenue becomes cash. A customer may delay payment because the invoice is incorrect, a shipment was incomplete, pricing does not match the agreement, product was damaged, or required documentation is missing.

What appears on the aging report as an overdue receivable may therefore have originated in order entry, shipping, customer service, pricing administration, or another part of the organization.

That is why receivables belong in an enterprise discussion.

Finance has an important role in credit and collections, but Sales, Operations, Customer Service, and management can all influence how quickly a sale ultimately becomes cash.

Growth makes this particularly important.

A company can add substantial revenue and simultaneously increase the amount of cash customers owe it. If the business is also moving toward larger accounts with longer terms, receivables can grow even faster than management expected.

The sales success is real.

So is the additional financial requirement.

Understanding that requirement while the customer and growth decisions are being made is very different from discovering it after the receivables have accumulated.

The other side of the working-capital cycle involves suppliers and the amount of time the company has before its own obligations must be paid.

## Accounts Payable Begins With Purchasing

Accounts payable is sometimes discussed as though it were simply the mirror image of receivables.

Customers owe the company money, while the company owes suppliers. From a financial perspective, that description is accurate.

From a management perspective, however, accounts payable reflects another set of decisions that begins before Finance schedules the payment.

The supplier relationship establishes much of the economics.

Purchasing chooses suppliers based on considerations that may include price, quality, reliability, lead time, availability, technical capability, and service. Payment terms are part of that relationship.

One supplier may require payment in fifteen days, another may offer thirty, and a third may provide sixty because of the company's volume, history, or negotiating position.

Those differences affect how long the company can retain cash before paying for the products and materials it purchases. In effect, supplier credit finances part of the operating cycle.

That does not mean suppliers should be treated simply as a source of free financing.

Strong supplier relationships can be strategically important, particularly for smaller businesses that depend on reliable access to products, materials, capacity, or favorable treatment during periods of shortage.

Stretching a critical supplier beyond agreed terms may improve cash temporarily while damaging a relationship that creates far greater value.

The more useful observation is that payment timing is part of supplier economics just as customer terms are part of sales economics.

A supplier offering the lowest price but requiring immediate payment may create a different financial requirement from a slightly more expensive supplier offering sixty-day terms. A vendor willing to provide favorable terms because of a long-standing relationship may create financial flexibility that is not obvious when management compares purchase prices alone.

Purchasing volume can affect the relationship as well.

Larger commitments may improve pricing or terms, but they can simultaneously increase inventory. Once again, the enterprise experiences all of the consequences together.

This is why accounts payable should not be reduced to the question of how slowly a company can pay its bills.

The more important management issue is how supplier selection, purchasing practices, negotiated terms, inventory decisions, and payment behavior work together.

When those decisions are considered alongside inventory and receivables, the enterprise nature of working capital becomes much easier to see.

## Working Capital Is an Enterprise Result

Imagine following one dollar through a product business.

The company commits that dollar when it purchases materials or inventory. The product may remain in stock for a period before it is sold. Once the sale occurs, the financial commitment may move into a receivable while the company waits for the customer to pay.

Supplier terms can postpone part of the company's own cash outlay during this cycle, but eventually the supplier has to be paid. Only when the customer pays does the cash complete its journey back into the company.

The length and financial requirements of that journey are determined by decisions made throughout the organization.

Purchasing influences how much inventory enters the business and under what supplier terms. Operations and Production influence how inventory moves and how much is required. Sales influences customer demand, pricing, terms, and commitments. Customer Service and other functions can affect whether invoices are paid without dispute. Finance manages credit, collections, payments, liquidity, and financial visibility.

No single function controls the entire cycle.

That is why attempts to improve working capital can become frustrating when management treats Inventory, Receivables, and Accounts Payable strictly as Finance responsibilities.

Finance can identify the numbers, highlight trends, establish financial discipline, and help leadership understand what is happening. It cannot independently change the commercial and operating decisions that created those numbers.

If inventory is increasing because Sales promises immediate availability across an expanding product range, the answer cannot come solely from Finance. If receivables are growing because the company is intentionally pursuing larger customers with longer terms, collections alone will not change the underlying requirement. If supplier terms are unfavorable because vendor decisions are made entirely around unit price, changing the payment schedule after the invoice arrives addresses only part of the economics.

Leadership has to see the operating cycle as a whole.

That does not mean the owner should become involved in every inventory purchase, customer negotiation, credit decision, or supplier payment. As a company grows, that level of involvement becomes impractical and eventually counterproductive.

What matters is that the people making those decisions understand how their objectives intersect and that management has enough visibility to recognize when the combined financial commitment is changing.

Working capital makes the cost of disconnected decisions particularly visible because the consequence appears directly in the amount of cash required to operate the business.

Revenue can grow, margins can remain attractive, and the company can be profitable while increasing amounts of cash become committed to Inventory and Receivables. Supplier credit may offset part of that requirement, but it rarely eliminates it entirely.

This is one reason successful product businesses can still feel financially constrained.

The business may be creating genuine economic value while continually reinvesting part of that value in the operating cycle.

That reinvestment may be entirely appropriate. The important issue is whether management understands why it is occurring, whether the amount is intentional, and whether the financial requirement remains consistent with the company's capacity and objectives.

That brings together the first seven Cash Flow Drivers we have examined.

Growth and Pricing influence the revenue the business chooses to pursue and the economics attached to it. Cost of Goods Sold and Operating Expenses reflect many of the decisions required to produce and support that revenue. Inventory, Receivables, and Accounts Payable determine how much financial capacity becomes committed inside the operating cycle and how long part of that capacity remains there.

They are different financial categories.

Inside the business, they are deeply connected.

The final three Cash Flow Drivers involve a different kind of decision. Rather than arising primarily from the normal commercial and operating cycle, they concern larger choices about where the company deliberately commits capital, how those commitments are financed, and how much of the cash generated by the business ownership chooses to retain.

Those decisions—Capital Expenditures, Debt, and Owner Distributions—can shape the financial position of the business for years.

That is where we turn next.

# CHAPTER 7

# Investment, Financing and Owner Capital Decisions

## CapEx Converts Cash Into Capability

The decisions we have examined so far arise largely from the normal commercial and operating activity of the business. Prices are negotiated, inventory is purchased, customers are extended credit, suppliers are paid, people are hired, and operating expenses are incurred. Those decisions can have substantial financial consequences, but many occur continually and can be adjusted as circumstances change.

Capital expenditures are different because they typically involve larger commitments intended to create value over a much longer period. When a company purchases a major piece of equipment, expands a facility, installs significant technology, or adds capacity, management is doing more than spending cash. It is converting financial capacity into a specific business capability.

A manufacturer purchasing a new production line may be creating greater capacity, improved efficiency, reduced labor requirements, better quality, or more reliable production. A distributor expanding a warehouse may be preparing for additional inventory, customers, products, or growth. A company implementing a new technology platform may be building capabilities intended to support a larger and more complex organization.

Those investments can create enormous value, but they also commit financial resources to a particular purpose. Once cash becomes equipment, a facility, automation, technology, or another long-term asset, that same cash is no longer available for another use unless the business generates or obtains additional capital.

That does not make the investment undesirable. Businesses have to commit resources in order to build capabilities, and some of the most valuable decisions an owner makes will require substantial cash before the full benefit becomes visible.

The important distinction is that a capital expenditure is not simply another payment. It is a decision about what the company believes it will need in the future and what it is willing to commit today to create that capability.

Consider a manufacturer purchasing additional production equipment. Management is making assumptions about future demand, capacity requirements, labor, maintenance, operating efficiency, product life, and how the business may develop over the useful life of the equipment. The investment may be supported by careful analysis, but the future remains uncertain.

Management is therefore committing resources today based partly on what it believes will happen tomorrow.

That is what makes significant capital expenditures different from many routine operating decisions. The commitment can be large, the decision may be difficult or expensive to reverse, and the expected economic benefit may unfold over years rather than months.

The relevant question is not simply whether the company has enough cash to make the investment. Leadership also needs to understand what capability the company is choosing to create, what assumptions support the decision, and what financial capacity will remain after the commitment has been made.

With capital expenditures, when the decision is made can matter almost as much as what management decides to buy.

## Timing Is Part of the Decision

Imagine a manufacturing company approaching the limits of its existing capacity. Demand has been increasing, equipment is running longer hours, overtime is becoming more common, and management believes another production line will eventually be necessary.

The question may no longer be whether additional capacity will ever be needed. The harder question is when to add it.

Investing now could allow the company to prepare ahead of demand, improve efficiency, reduce pressure on existing equipment, and avoid disappointing customers if growth continues. Waiting could preserve cash, provide more time to confirm demand, and reduce the risk of committing capital to equipment that remains underutilized if growth develops more slowly than expected.

Both alternatives carry risk. Investing too early can leave the company carrying the financial burden of excess capacity before it needs it. Investing too late can create excessive overtime, service problems, production bottlenecks, equipment failures, or lost opportunities the organization cannot support.

The same issue appears with replacement decisions. An older machine may still be operating, but maintenance costs are rising and downtime is becoming more frequent. Replacing it requires a meaningful investment today, while continuing to operate it preserves cash but exposes the company to the possibility of additional repairs, production interruptions, quality problems, or failure at an inconvenient moment.

What makes these decisions difficult is that the cost of investing is usually visible and immediate, while much of the cost of waiting is uncertain. Management knows what the new equipment will cost. It cannot know with the same precision what a production interruption, capacity constraint, or missed customer opportunity might eventually cost.

Technology creates a similar tension. Implementing a new system too early may mean spending money before the organization genuinely needs the capability. Waiting too long may force the company to make the transition after existing processes are already breaking under greater complexity.

Management can therefore make a sound decision about what the company eventually needs and still make a poor decision about when to commit the resources.

This does not mean every capital expenditure requires an elaborate analysis. Smaller investments deserve proportionally less scrutiny than large, difficult-to-reverse commitments. The underlying principle is simply that timing is part of the economics.

Sometimes the right decision will be to invest before the need becomes urgent. In other situations, preserving financial capacity while management waits for greater certainty will be the better choice.

Either way, leadership is making a judgment about the future and deciding when the expected benefits justify converting financial capacity into a particular business capability.

If the company does not want to fund that investment entirely with existing cash, another important decision follows: how should it be financed?

## Debt Creates Capacity—and Commitments

Debt often attracts strong opinions. Some owners view borrowing primarily as a source of risk and prefer to avoid it whenever possible, while others consider debt an important tool for accelerating growth and preserving internally generated cash.

Both perspectives can be reasonable because debt itself is neither inherently good nor inherently bad. It is a financing instrument, and its value depends largely on why the company is borrowing, what the financing allows the business to accomplish, and whether future cash flow can comfortably support the obligation.

Used appropriately, debt can allow a business to pursue opportunities that would otherwise be delayed or unavailable. Companies borrow to finance equipment, facilities, acquisitions, inventory, seasonal requirements, and working-capital needs. For many successful businesses, debt is a normal and productive part of the capital structure.

The important distinction is that borrowing creates financial capacity today while establishing claims on future cash flow.

Suppose a company borrows $1 million to purchase equipment. The financing allows the business to acquire the equipment without immediately consuming $1 million of existing cash, which may preserve liquidity for inventory, payroll, growth, or other operating requirements.

In exchange, the company commits future cash to principal and interest payments. If the equipment generates the expected improvements in capacity, productivity, or economics, the future cash produced by the investment may comfortably support the debt. If the investment underperforms, however, the loan payments do not disappear. The business still has to meet those obligations from cash generated elsewhere.

The financing decision therefore cannot be separated completely from the business decision being financed.

Working-capital borrowing creates a similar relationship. A line of credit can be an extremely useful tool for managing timing differences between inventory purchases, customer collections, and supplier

payments. A seasonal business may borrow while inventory is being built and repay the line after customers pay. A growing business may use borrowing to finance increasing working-capital requirements while revenue expands.

Those can be entirely appropriate uses of debt.

The management issue becomes more complicated when borrowing begins financing a requirement the company does not fully understand. Suppose the balance on a company's line of credit increases year after year. Management may conclude that a larger company simply needs a larger credit facility, and that may be true.

But the growing borrowing requirement might also reflect Inventory increasing faster than sales, customer terms lengthening, margins weakening, Operating Expenses expanding, larger Owner Distributions, or several of those conditions occurring together.

A line of credit can supply the cash needed to fund those decisions without explaining why the requirement exists. As long as additional borrowing capacity remains available, the underlying pattern may continue without creating an immediate crisis.

Eventually, however, additional borrowing may no longer be available.

My Valentine's Day experience as a new CFO made that reality very tangible. By the time I received the phone call that we could not make payroll, available borrowing capacity was essentially exhausted. The immediate problem was cash, but simply asking for more debt was no longer a meaningful answer.

The lesson I carried forward was not that borrowing should be avoided. Debt can create valuable financial capacity, but it also creates an obligation that future cash flow has to support.

Management therefore needs to understand what the debt is financing, what assumptions support the borrowing decision, and what future cash generation will be required to meet the obligation.

The same capital-allocation responsibility applies when cash leaves the company for an entirely different reason: it goes to the owners.

## Owner Distributions Are Business Decisions Too

One of the reasons people build businesses is to create economic value for themselves and their families. Owners invest capital, accept risk, guarantee obligations, endure uncertainty, and frequently spend decades building an asset that becomes a significant part of their personal financial position.

There is nothing inherently inappropriate about taking money out of a successful business. Owner distributions are one of the legitimate economic returns of ownership.

The decision question is not whether distributions are good or bad. It is how the distribution fits with the other financial requirements and objectives of the business.

This can become complicated because accounting profit and available cash are not the same thing. A company may report an attractive profit while simultaneously investing heavily in Inventory and Receivables to support growth. Equipment may need to be replaced, debt may have to be repaid, or management may be preparing for a major future investment.

The business has created economic value, but much of the associated cash may still be committed elsewhere.

An owner looking only at net income can therefore reach a very different conclusion about how much cash is available for distribution than the company's overall financial position supports.

The opposite situation can occur as well. A mature company with modest growth, strong margins, efficient working capital, limited debt, and relatively few capital requirements may consistently generate more cash than it needs to operate and reinvest. Retaining every dollar indefinitely simply because more cash feels safer may not serve the owner's objectives either.

There is no universal percentage of profit that owners should distribute.

The appropriate decision depends on the economics, risks, growth plans, working-capital needs, capital requirements, debt obligations, and financial strength of the particular business, along with the legitimate objectives of ownership.

What matters for this discussion is recognizing that distributions are part of capital allocation. Cash distributed to an owner is no longer available inside the company for equipment, debt reduction, inventory, growth, acquisitions, reserves, or other purposes.

That does not mean the distribution should not happen. It means the owner should understand what financial capacity leaves the enterprise when it does.

Owners can sometimes think about distributions differently from other uses of cash because the money is effectively moving from a company they own to themselves. Economically, however, the business still has less cash afterward.

That creates a genuine tradeoff when personal and business objectives compete. An owner may want to diversify personal wealth, prepare for retirement, make investments outside the company, support family objectives, or simply enjoy part of the economic reward created by years of ownership.

At the same time, the business may need capital for working capital, equipment, debt reduction, resilience, or future growth. There is no reason to assume those objectives will always align perfectly.

Good ownership requires deciding how to balance them.

That brings CapEx, Debt, and Owner Distributions together around one central capital-allocation principle.

## Every Yes Has an Opportunity Cost

Every business has multiple potential uses for its financial resources. Management may want to purchase equipment, add capacity, reduce debt, make an acquisition, increase inventory, invest in technology, develop a new product, or retain financial capacity for opportunities and risks that have not yet appeared.

Ownership may also reasonably decide that some of the cash generated by the business should leave the company through distributions.

Each can be a legitimate use of capital, but the same dollar cannot support all of them simultaneously.

A dollar invested in equipment cannot also reduce debt. Cash used for an acquisition cannot remain available as a reserve. Money distributed to ownership is no longer available to finance additional working capital. Conversely, cash retained inside the company preserves financial capacity but may mean postponing an investment capable of creating substantial value.

That is the opportunity cost embedded in capital allocation.

Recognizing that tradeoff does not mean management should become reluctant to commit resources. Businesses create value by making commitments. They invest in capability, assume appropriate risks, use financing intelligently, and return economic value to ownership.

The objective is not to preserve every option forever. It is to understand what the company is choosing when it commits the resources and what alternatives become less available afterward.

This is broader than simply asking whether the company has enough cash to make a purchase or distribution. A business may technically have enough money and still conclude that another use of the financial capacity is more important.

Likewise, a company may decide to borrow rather than use available cash because preserving liquidity has greater strategic value than avoiding debt. Another company may reach the opposite conclusion because reducing leverage is currently more important than maintaining excess cash.

There is no universal answer because capital allocation is fundamentally about priorities.

An owner-led company does not need the formal investment committees or elaborate capital-allocation processes found in large corporations to apply this principle. Leadership simply needs to recognize that every meaningful capital decision places a claim on the financial resources of the business.

CapEx converts financial capacity into capability. Debt creates capacity today while establishing future obligations. Owner Distributions transfer financial resources from the enterprise to ownership.

Each can be exactly the right decision, and each changes what remains available for everything else.

With this chapter, we have now examined all ten primary Cash Flow Drivers used throughout this guide: Growth, Pricing, Cost of Goods Sold, Operating Expenses, Inventory, Receivables, Accounts Payable, Capital Expenditures, Debt, and Owner Distributions.

We have examined them separately because separating the decisions makes their individual financial consequences easier to see.

The business itself does not experience them separately.

A growth decision can affect Inventory, Receivables, Operating Expenses, and eventually CapEx. A capital investment may require Debt. A purchasing decision can influence COGS, Inventory, and Accounts Payable. An Owner Distribution changes the financial capacity available to support decisions throughout the enterprise.

Those relationships are important enough that they deserve more than a passing mention.

Once management understands the individual decisions behind cash flow, the next step is understanding how those decisions interact—and how one seemingly isolated decision can trigger consequences across several Cash Flow Drivers at once.

That is where we turn next.

# CHAPTER 8

# Decisions Don't Happen in Isolation

## One Decision Creates Another

Over the last four chapters, we have examined the ten primary Cash Flow Drivers separately because separating them makes it easier to see the decisions behind each one. Growth, Pricing, Cost of Goods Sold, Operating Expenses, Inventory, Receivables, Accounts Payable, Capital Expenditures, Debt, and Owner Distributions appear as distinct financial categories, and each gives management a useful way to understand one part of the business.

The business itself does not experience them separately.

A decision involving one driver frequently changes another, and sometimes the connection is obvious while in other cases the financial consequence appears somewhere far removed from the original decision. That is why understanding the individual drivers is only the first step. Management also has to understand how those drivers interact.

Growth provides perhaps the clearest example. A company decides to pursue a significant increase in revenue, and if the plan succeeds, additional sales may require more Inventory, larger Receivables, additional employees, higher Operating Expenses, greater warehouse or production capacity, and eventually additional capital investment. If internally generated cash is not sufficient to support those requirements, borrowing may increase as well.

The original decision was about growth, but the financial consequences can appear across half the business.

Pricing decisions create their own chain of effects. A price reduction may increase volume, which could improve production efficiency or purchasing economics, but greater volume may also require more Inventory, Receivables, labor, freight, or capacity. A price increase can create the opposite pattern. The company may generate more margin on each unit while experiencing some reduction in volume, potentially reducing working-capital or capacity requirements at the same time.

Neither result can be understood completely by looking at price alone.

Purchasing decisions are equally interconnected. A larger order may reduce unit cost and improve supplier economics while simultaneously increasing Inventory. More favorable supplier terms may offset part of the cash requirement through Accounts Payable. A different supplier may offer a lower price but require larger minimum orders, longer lead times, or more inventory protection.

Capital expenditures can affect several drivers as well. New equipment may reduce operating costs, increase capacity, improve quality, or allow the business to support future growth. If the equipment is financed, the same decision also affects Debt and future cash obligations.

Even Owner Distributions, which may appear separate from day-to-day operations, influence what happens elsewhere. A distribution does not change the economics of Inventory or Receivables directly, but it changes the amount of internally generated capital available to support them.

This interconnectedness is why the ten drivers should not be thought of as ten independent levers that management simply pushes in whatever direction appears most favorable to cash. Reducing Inventory may release cash, but reducing it too aggressively could undermine availability or customer service. Extending Accounts Payable may preserve cash temporarily, but stretching important suppliers beyond agreed terms can damage relationships the company depends upon. Avoiding Debt may reduce financial risk while also preventing an attractive investment from being made at the right time.

The better management question is not simply whether one driver should move up or down. It is what else changes when management makes the decision.

That is where the financial consequence of one choice begins to move through the enterprise.

## The Domino Effect

Consider a hypothetical product business that has an opportunity to win a large new customer. The account could add approximately $2 million of annual revenue, provide credibility in an important market, and create opportunities with other customers.

Sales has worked hard to develop the relationship, and management believes winning the account would represent meaningful progress for the company. The customer, however, has requirements.

To win the business, the company agrees to somewhat lower pricing than it receives from many existing customers. The customer expects sixty-day payment terms rather than the company's more typical thirty days, and it also requires high product availability because stockouts could jeopardize the relationship.

None of those concessions necessarily makes the account unattractive. The expected volume may more than justify them.

Once management says yes, however, several things begin happening at the same time.

Sales increases, but because the customer expects dependable availability, Inventory also increases before all of the new revenue has been generated. The company begins committing cash to support sales that have not yet occurred.

When products ship, Receivables increase as well. The customer is paying according to the agreed sixty-day terms, but the company now waits longer for the cash to return than it does with many existing customers.

Operations becomes busier. Overtime increases initially, and management eventually concludes that another employee is needed. Operating Expenses rise.

Purchasing sees the increased volume and negotiates better pricing from a supplier, improving COGS. To obtain the best economics, however, the company accepts larger order quantities, adding another layer of Inventory.

Several months later, the new account is growing faster than expected. That is good news, but existing warehouse capacity is becoming tight, and management begins considering additional racking, material-handling equipment, or expanded space.

What began as a customer decision is now influencing Growth, Pricing, Inventory, Receivables, COGS, Operating Expenses, and potentially CapEx. If the additional requirements exceed the cash being generated internally, the company's line of credit may increase as well, bringing Debt into the chain.

Nothing in this hypothetical necessarily suggests that management made a poor decision. The new customer may become one of the most valuable relationships the company has ever developed.

The important point is that the business did not receive the revenue by itself. It received the full chain of operating and financial consequences attached to the decision.

This is where owners can become frustrated when they look at the financial results several months later. Revenue may be up substantially. Gross profit may be higher, and the company may be more strategically important in its market. Yet cash may be tighter than expected.

If management looks only at the final cash result, the situation can seem contradictory. When leadership follows the decision chain, however, the explanation becomes much clearer: the company deliberately committed resources to support an opportunity.

The more important question is whether management understood those commitments when the decision was made and whether the expected value of the opportunity continues to justify them.

A different scenario can begin with what appears to be a much smaller operating decision. Suppose Purchasing receives an opportunity to reduce the cost of an important component by five percent if the company doubles its normal order quantity.

The savings are attractive, and the component is used regularly. Purchasing recommends accepting the offer.

The immediate effect is favorable because unit cost declines, but the larger order also increases Inventory. If the company uses the material more slowly than expected, the cash remains committed longer. Additional warehouse space may be required, or other products may become more difficult to store efficiently.

If the purchase is significant enough, the company may use more of its line of credit temporarily, increasing interest expense. If demand later changes or the product is modified, management may discover that some of the inventory is no longer as valuable as originally expected.

Again, none of this proves that the purchasing decision was wrong. The five-percent savings may still make the larger order economically attractive.

What matters is recognizing that the decision did not remain inside Purchasing or COGS. Its consequences moved into Inventory, financial capacity, and potentially Debt.

That is the domino effect: one decision changes another condition, which creates another requirement, which eventually becomes visible somewhere else in the financial results.

The larger and more complex the company becomes, the harder those connections can be to see.

That is where organizational silos become particularly important.

## The Silo Problem

Every function inside a business sees the company through a somewhat different lens. That is not a flaw. It is one of the reasons organizations create specialized functions in the first place.

Sales understands customers, competitors, markets, and commercial opportunities. Purchasing understands suppliers, sourcing alternatives, lead times, and purchase economics. Operations understands production, capacity, service requirements, quality, and the practical realities of delivering what the company sells. Finance understands profitability, working capital, liquidity, financing, and the financial consequences appearing across the organization.

Each perspective is valuable.

The problem arises when a decision crosses boundaries that are invisible to the person making it.

A salesperson negotiating sixty-day terms may understand exactly why those terms are necessary to win an important account. What may be less visible is the amount of additional working capital required if several large customers receive similar terms.

Purchasing may see a compelling volume discount without having complete visibility into the other inventory commitments already developing throughout the business. Operations may reasonably want additional safety stock to protect customer service while being unaware that Sales has just negotiated several customer relationships requiring even more dedicated Inventory.

Finance may see Inventory and Receivables rising and conclude that working capital needs attention without fully understanding the customer-service, supply-chain, or growth decisions driving the increase.

Nobody has to be incompetent for this to happen. In fact, everyone can be doing a good job within the boundaries of their responsibilities.

The difficulty is that departmental boundaries do not contain the financial consequences of departmental decisions.

This is the same distinction between functional optimization and enterprise optimization we introduced earlier in the guide, but after examining all ten Cash Flow Drivers, we can now see more clearly why the distinction matters.

Sales cannot reasonably optimize only revenue if the economics of the customer relationship undermine the enterprise. Purchasing cannot optimize only unit cost if the decision creates disproportionate inventory requirements. Operations cannot optimize only availability without considering the financial capacity required to provide it.

Finance cannot optimize only near-term cash either. A decision that consumes cash today may create significant value tomorrow.

Every function has a legitimate objective, but the enterprise has to live with all of them together.

That creates a leadership responsibility that becomes more important as the business grows and decision-making becomes increasingly distributed.

## Someone Has to See the Whole Business

In a very small company, the owner may personally participate in nearly every meaningful decision. The same person can be involved in selling to customers, negotiating with suppliers, approving purchases, hiring employees, managing cash, and deciding when to invest.

As the company grows, that becomes impossible.

Responsibility has to spread across the organization. Salespeople negotiate with customers. Purchasing makes supplier decisions. Operations manages production and Inventory. Department leaders hire people and commit resources. Finance manages financial visibility and liquidity.

That distribution of decision-making is necessary for growth, but it also means no single manager may naturally see the complete financial effect of everything being decided throughout the company.

Someone still has to see the whole business.

That responsibility ultimately belongs to ownership and senior leadership, supported by Finance and the managers who understand the operating realities behind the numbers.

This does not mean every decision should be elevated to the owner. Requiring senior approval for every discount, purchase order, inventory adjustment, hire, or customer exception would slow the organization and undermine the management capability the company needs in order to grow.

The objective is not centralized decision-making. It is enterprise visibility.

Leadership needs to identify which decisions are significant enough to deserve a broader view and create an environment in which managers understand that their choices can have consequences beyond their own functional objectives.

That may mean Sales and Finance discuss the economics of a major customer before unusual terms are finalized. Purchasing and Operations may evaluate a large Inventory commitment together rather than focusing separately on unit cost and availability. Management may consider several planned hires, capital investments, and growth initiatives collectively rather than approving each one independently over several months.

The exact process will vary with the size and complexity of the business.

The principle does not.

Significant decisions should be understood in the context of the enterprise rather than solely through the function where they originate.

That requires communication across functions, but it also requires something else: a common way of discussing consequences.

Cash flow can provide part of that common language.

## Cash Flow as a Common Language

Different functions will not always agree about what the business should do, nor should they.

Sales may believe a major customer opportunity deserves aggressive terms. Finance may be concerned about the working-capital requirement. Operations may worry about capacity. Purchasing may see opportunities to improve economics if volume increases.

Those perspectives represent different responsibilities, and a healthy management discussion should allow them to surface.

The purpose of cash-flow awareness is not to make every function think like Finance. It is to give the organization another shared question:

**What does this decision require from the business financially?**

That question does not determine whether the decision should be approved.

A decision can require substantial cash and still be exactly the right thing to do. Growth may deserve investment. Inventory may need to increase. A strategically important customer may justify longer terms. Equipment may need to be purchased before existing capacity is exhausted.

The value of the question is that it makes the financial commitment visible alongside the operational and strategic benefits.

Sales can still argue for the customer. Operations can still argue for capacity. Purchasing can still argue for better economics. Finance can still raise concerns about liquidity and financial capacity.

Leadership can then evaluate the complete decision rather than allowing one functional perspective to dominate the others.

This is particularly important because cash flow provides a point of convergence among decisions that otherwise look unrelated. A new customer, a larger Inventory order, another employee, an equipment purchase, and an Owner Distribution may originate in completely different parts of the business.

Financially, however, they all compete for some portion of the company's available capacity.

Looking at those decisions through a common cash-flow lens helps management see the cumulative commitment before every consequence appears in the financial statements.

That does not eliminate uncertainty, and it does not guarantee that management will make the right decision every time. Businesses operate with incomplete information. Customers change their minds. Forecasts miss. Suppliers encounter problems. Markets shift. Investments perform differently than expected.

The objective is not perfect foresight. It is better visibility into the consequences management can reasonably anticipate before the company commits itself.

That is the progression we have been building throughout this guide.

Cash flow is a management result because decisions throughout the company help create it. Financial numbers can be traced backward to the decisions and assumptions behind them. Individually rational decisions can produce unintended enterprise consequences, and the ten primary Cash Flow Drivers provide a way to see where those consequences become financially visible.

Now we add another layer: those ten drivers are interconnected.

A decision made in one part of the business can create financial consequences somewhere else, and several individually attractive decisions can compete for the same financial capacity.

Once leadership sees those connections, the next challenge is practical.

How do we improve the quality of important decisions without slowing the business down or turning every management discussion into a financial analysis?

The answer begins with better questions.

# CHAPTER 9

# Better Decisions Begin With Better Questions

## What Happens to Cash?

Business decisions are rarely made with perfect information. Owners do not know exactly how much a new customer will eventually buy, whether a product launch will meet expectations, how quickly a new employee will become productive, or whether a capital investment will create precisely the economics management expects.

Decisions still have to be made.

The objective, therefore, is not to create a formula that produces the correct answer every time. No such formula exists. The more practical objective is to improve what management can see before the company commits itself.

Chapter 8 showed why that matters. A decision made in one area can create consequences throughout the enterprise. A new customer can influence Pricing, Inventory, Receivables, Operating Expenses, and capacity. A purchasing decision can affect COGS, Inventory, Accounts Payable, and financial capacity. A capital investment may improve operations while creating Debt and future cash obligations.

Once those connections become visible, owners and managers need a practical way to bring them into the decision itself.

That begins with a simple question:

**What happens to cash if we do this?**

That question is different from asking whether the decision is profitable. Profitability matters, of course, but an economically attractive decision can still require substantial cash before the expected value appears.

Suppose a company has an opportunity to add a major customer. Management estimates that the account will generate $1.5 million in annual revenue at an acceptable margin. From a sales and profit perspective, the opportunity may look very attractive.

The cash question broadens the conversation. How much Inventory will need to be available before sales occur? What payment terms will the customer receive? Will additional people or capacity be required? How much of the company's financial resources will be committed before the cash from the new revenue returns?

Those questions do not weaken the case for pursuing the customer. They simply tell management more completely what it is saying yes to.

The same principle applies to equipment. Management may determine that a new machine will reduce labor, increase output, improve quality, or relieve an important capacity constraint. The investment may make excellent economic sense, while the cash question asks what resources the company must commit today to obtain those benefits tomorrow.

This is why one of the simplest recurring management questions in the book may also be one of the most useful. In addition to asking whether a decision will make money, leadership should ask what that decision requires from cash.

Once management asks that question, timing becomes impossible to ignore.

## When Does the Cash Leave—and When Does It Return?

Timing can change the financial character of an otherwise attractive decision. A company may make a profitable sale and wait sixty days to receive the cash. Inventory may be purchased three months before it is sold. A salesperson may be hired months before enough new revenue develops to cover the cost, while equipment may require a substantial payment today even though the productivity benefits appear gradually over several years.

In each case, the economics and the cash timing are different.

This is especially important in product businesses because cash frequently leaves before revenue arrives. Consider a company preparing for a large seasonal selling period. Inventory may have to be purchased months in advance so the product is available when customers need it.

If the season performs as expected, the investment may produce excellent revenue and profit. During the months before customers pay, however, the business still has to finance that Inventory and every other obligation continuing alongside it.

The decision can be economically attractive and financially demanding at the same time.

Growth creates the same issue. A company may correctly identify an opportunity to expand sales by 20 percent, but supporting that increase can require Inventory, Receivables, people, and operating capacity before the resulting cash is fully collected.

Management therefore needs to understand not just how much cash a decision requires, but when the requirement appears relative to the expected return. That does not mean every decision needs a detailed cash-flow forecast. A modest commitment may require only a few minutes of thought, while a major investment, new market, acquisition, or large customer may deserve considerably more analysis.

The level of effort should match the significance and reversibility of the decision.

The underlying management principle is straightforward. If cash leaves substantially before it returns, the company has to finance the gap. That financing may come from internally generated cash, supplier terms, a line of credit, other borrowing, or additional owner capital.

Any of those approaches may be appropriate. What matters is that the timing requirement becomes visible before the commitment is difficult to change.

This is one reason decisions can look very different on paper from the way they feel inside the business. Profit may eventually appear exactly as expected while the company experiences months of financial pressure because cash is moving on a different schedule.

Understanding timing makes the decision more complete, but management also needs to understand what other commitments may come with it.

## What Else Does This Decision Commit Us To?

A business decision rarely arrives alone. A new customer brings more than revenue. A piece of equipment brings more than a purchase price. A new employee brings more than salary, and growth brings more than additional sales.

Each can create secondary commitments that are easy to underestimate when management focuses primarily on the immediate objective.

Consider the large-customer example again. Sales may be focused appropriately on the revenue opportunity, but serving the account could also require dedicated Inventory, longer customer terms, specialized packaging, technology integration, additional customer-service support, expanded production capacity, or increased warehouse activity.

The customer does not enter the company alone. The relationship brings requirements with it.

Equipment works the same way. The purchase price may be the most visible commitment, but installation, tooling, training, maintenance, software, facility modifications, additional people, or increased working capital may follow.

Hiring also creates secondary consequences. Compensation is only the beginning. Benefits, systems, workspace, supervision, travel, training, administrative support, and other resources may become part of the economic commitment.

Identifying those additional requirements does not automatically make the decision less attractive. Leadership may conclude that the complete commitment is larger than originally expected and still believe the anticipated value more than justifies it.

The discipline lies in seeing the complete commitment before saying yes.

This becomes particularly important in growing businesses because opportunities can arrive faster than financial and organizational resources expand. Sales may want additional Inventory while Operations wants equipment, management wants to hire, and another initiative requires technology or marketing.

Each proposal may look affordable when evaluated separately. The enterprise has to support them collectively.

That was one of the central lessons of Chapter 8. Here, it becomes a practical decision question: **What else are we committing to if we do this?**

Looking beyond the immediate commitment also exposes something more fundamental. Every important business decision contains assumptions about what management believes will happen next.

## What Has to Be True?

Business decisions are bets on the future, even when they are supported by excellent information, substantial experience, and careful analysis. Management makes decisions because it believes certain conditions are likely to develop, but the future remains uncertain.

A company increases Inventory because management expects demand to support it. A business hires several employees because leadership believes the organization will need additional capacity. A manufacturer purchases equipment because management expects future demand and operating improvements to justify the investment.

Customer decisions contain assumptions as well. Management may expect an account to buy a certain amount, purchase a particular product mix, pay according to agreed terms, and require a manageable level of service. The pricing and concessions offered during the negotiation may make excellent sense if those assumptions prove reasonably accurate.

There is nothing wrong with making assumptions. Decisions would be impossible without them.

The problem is that assumptions often disappear from view once the decision has been made. Six months later, management sees excess Inventory but may no longer remember that the original purchase was based on a sales forecast that failed to materialize. A new employee appears expensive relative to current revenue, but the hiring decision assumed an expansion that was delayed.

Equipment may be underutilized even though the original investment was based on customer demand expected to develop much faster. The financial consequence remains visible while the assumption that created it fades into the background.

That is why one of the most useful questions management can ask before a significant commitment is:

**What has to be true for this decision to work the way we expect?**

Perhaps volume has to reach a certain level. A price increase may need to hold. Demand may need to materialize within a particular period, a productivity improvement may need to occur, or a customer or supplier may need to behave as expected.

Making those assumptions visible does not make them correct. It allows management to recognize what the decision depends upon and later compare those assumptions with reality.

If Inventory was increased in anticipation of growth, management can watch whether that growth develops. If customer economics depend on a certain level of volume, leadership can observe whether

the account is actually purchasing at that level. If equipment was justified by productivity improvements, the company can determine whether those improvements are appearing.

This is not about building elaborate measurement systems around every decision. It is about understanding what management is relying on when it commits the company's resources.

Once those assumptions are visible, another question becomes possible: what happens if they do not develop as expected?

## What Happens If We're Wrong?

Optimism is part of entrepreneurship. People do not build companies, enter new markets, develop products, hire employees, buy equipment, and pursue growth because they believe nothing will work.

Owners have to believe opportunities are worth pursuing. Financial discipline should not replace that optimism with pessimism; it should make room for uncertainty.

Suppose a company builds additional Inventory because management expects demand to increase substantially. If the growth arrives as planned, the Inventory supports the opportunity and may allow the company to serve customers exceptionally well.

But if demand arrives six months later than expected, the company has to carry that Inventory longer. If some of the expected demand never materializes, management may face a different set of questions about how easily the product can be sold elsewhere, consumed gradually, returned, or repurposed.

Hiring ahead of growth creates a similar issue. If revenue develops as expected, management may be pleased that the organization built capability before it was desperately needed. If growth is delayed, the company has to determine how long it can comfortably carry the additional Operating Expense.

Capital expenditures deserve the same thinking. Management may expect a project to cost $750,000, be operational in six months, and produce a certain level of efficiency. If installation takes nine months, costs another $100,000, or produces only part of the expected improvement, the business needs enough financial flexibility to absorb the difference.

This is not an argument for constructing worst-case scenarios around every decision. It is an argument for understanding the company's margin for error.

Two companies can pursue the same opportunity with very different levels of financial risk because their underlying capacity differs. A business with strong cash generation, manageable Debt, adequate liquidity, and borrowing capacity may be able to tolerate an investment developing more slowly than expected. Another company operating close to its financial limits may need almost everything to happen according to plan.

The opportunity may be identical. The company's ability to absorb being wrong is not.

That distinction matters because business decisions rarely fall neatly into two categories—success or failure. More often, results simply develop differently from the original expectation. Revenue takes

longer, costs are somewhat higher, customers pay more slowly, implementation becomes more difficult, or productivity improves less quickly than anticipated.

Management does not need certainty before making a decision. It needs enough visibility to understand how much flexibility remains if expectations are not met.

That leads directly to another question we introduced in Chapter 7: what alternatives become less available when the company commits its resources?

## What Options Are We Giving Up?

Every meaningful commitment has an opportunity cost. Chapter 7 addressed this directly in the context of CapEx, Debt, and Owner Distributions, but the principle applies far more broadly.

Cash committed to Inventory cannot simultaneously fund equipment. Financial capacity supporting a new customer is not available for another opportunity. Additional borrowing used to finance growth reduces some of the debt capacity that might otherwise be available later, while hiring several people today changes the recurring cost structure management carries into tomorrow.

None of those consequences means the commitment is wrong. Businesses cannot create value while preserving every alternative indefinitely.

At some point, management has to choose.

The decision question is whether leadership understands what alternatives become less available after that choice has been made.

This becomes especially important when several attractive opportunities compete for the same financial capacity. Imagine a company with $1 million of reasonably available financial resources. Management is considering a $600,000 equipment investment, Sales wants to build $300,000 of additional Inventory to support several new accounts, and the owner is considering a significant distribution after a profitable year.

Each use of cash may be entirely reasonable. Collectively, however, they require more financial capacity than the company has available without additional financing.

The question cannot be answered simply by evaluating each proposal independently. Leadership has to establish priorities.

Perhaps the equipment is strategically essential and the distribution can wait. Perhaps the Inventory opportunity produces the greater near-term value and the equipment should be postponed. Management may decide to proceed with both and finance part of the requirement.

There is no universal answer because capital allocation is ultimately about choices among competing priorities.

The value lies in seeing those choices before the resources have been committed separately over several months.

This is also one of the important connections between this guide and *Cash Flow Creates Options*™. Stronger financial capacity creates more possible courses of action. Every significant commitment converts some of that general flexibility into a specific decision.

That is not a reason to preserve cash indefinitely. It is a reason to understand what management is choosing to do with it.

By this point, the decision conversation has become considerably richer. Management has considered what happens to cash, when cash leaves and returns, what additional commitments accompany the decision, what assumptions have to be true, what happens if those assumptions are wrong, and what alternatives become less available.

None of those questions automatically tells management whether the answer should be yes or no.

That is why the final question brings them together.

## Would We Still Make the Decision?

There is a danger in turning good management questions into another checklist. That is not the objective here.

An owner-led company should preserve one of its greatest advantages: the ability to make decisions quickly. Managers should not need lengthy financial analyses every time a customer asks for something unusual, a supplier presents an opportunity, or Operations needs to solve a problem.

Some decisions require minutes, while others deserve hours, days, or weeks. The level of thought should be proportionate to the size, duration, complexity, and reversibility of the commitment.

What matters is that management sees enough of the decision to understand what it is agreeing to.

That brings the discussion to a final question:

**Would we still make this decision if we could see its full cash consequence today?**

Sometimes the answer will be an immediate yes. Management may understand that a new customer requires substantial Inventory and Receivables, that the margins are somewhat lower than normal, and that additional capacity will eventually be necessary—and still conclude that the opportunity is excellent.

That is a better yes because leadership understands more of what it is choosing.

In another situation, the answer may still be yes, but with a change in timing, scope, financing, or terms. Perhaps the company proceeds with the equipment but delays another investment. It wins the customer but negotiates different terms, hires one person today rather than three, or purchases enough

Inventory to support the immediate opportunity while waiting for additional demand before making the next commitment.

Sometimes the answer will be no because a decision that appeared attractive through one functional lens looks different once management sees the complete enterprise requirement.

That is not financial conservatism. It is better decision-making.

The objective is not to make decisions that always improve short-term cash. Some of the best business decisions will consume cash, increase working capital, add Debt, raise Operating Expenses, or require substantial investment before the economic benefits appear.

The objective is to make those decisions with greater visibility into their consequences.

Better questions move the cash-flow conversation upstream, while management still has choices. They expose commitments that might otherwise become visible only after the financial result appears, make assumptions easier to recognize, and help leadership understand how much uncertainty the company is prepared to absorb.

Most importantly, they reinforce the central premise of this guide. Cash flow may be the financial result, but the decisions creating that result come first.

If management wants greater influence over tomorrow's financial position, the best opportunity is not after the numbers arrive. It is while today's important decisions can still be shaped.

Better questions improve individual decisions. The larger challenge is making that way of thinking part of how the business is managed.

That is where we turn next.

# CHAPTER 10

# From Cash Flow Management to Decision Management

## Stop Managing Only the Result

Most businesses manage cash flow primarily through financial information.

They monitor bank balances, review cash reports, prepare forecasts, manage Receivables, track Inventory, evaluate borrowing requirements, and look ahead to major expenditures. Those activities are essential, particularly as a company becomes larger and more complex.

A business that does not know where it stands financially is taking unnecessary risk.

Nothing in this guide changes that.

Finance still needs reliable reporting. Leadership still needs forecasts. Receivables have to be collected, obligations have to be paid, liquidity has to be monitored, and financing requirements have to be anticipated.

The limitation is that most of those activities deal with consequences that have already been created—or with financial consequences expected to emerge from decisions already being made.

A bank balance tells management where the company stands today.

A cash-flow forecast attempts to show where existing plans and assumptions may take the business tomorrow.

A working-capital report reveals what has already become committed to Inventory and Receivables and what is being financed through Accounts Payable.

All of that information matters.

But by the time many of those numbers become visible, the business may already have made the decisions that largely determined them.

A customer may already have received sixty-day terms.

Inventory may already have been ordered.

People may already have been hired.

Equipment may already have been purchased.

A growth initiative may already be underway.

Debt may already have been incurred.

Cash may already have been distributed to ownership.

Finance can help management respond to the consequences of those decisions, but it cannot travel backward and make the original decision again.

That is the distinction this entire guide has been building toward.

Cash-flow management should not stop at managing the result.

It should also influence the decisions creating the result.

That does not mean every cash-flow problem could have been prevented if management had simply thought harder. Businesses operate in uncertain environments, and external circumstances can overwhelm even well-considered plans.

Customers fail.

Markets change.

Costs move unexpectedly.

Suppliers experience disruptions.

Demand develops differently from forecasts.

The objective is not to create a business in which cash flow never surprises anyone.

The objective is to stop treating cash flow primarily as something management deals with after the financial consequences have already become difficult to change.

The opportunity begins earlier.

It begins upstream.

## Move Upstream

Chapter 2 introduced the idea of following the decision trail backward.

If Inventory increased, management could ask what changed in forecasting, purchasing, product assortment, customer requirements, production, or supplier economics. If Receivables expanded, leadership could look behind the financial number to customer selection, terms, credit decisions, commercial practices, or operating problems affecting payment.

That backward-looking process helps management understand today's financial position.

The more powerful application is forward-looking.

If yesterday's decisions created part of today's cash flow, then today's decisions are already beginning to create tomorrow's.

That means the best time to understand the cash consequence of an important decision is while the decision can still be changed.

Before the customer terms have been finalized.

Before the Inventory has been purchased.

Before the employee has been hired.

Before the equipment has been ordered.

Before the Debt has been incurred.

Before the distribution has been made.

At that point, management still has options.

The company may proceed exactly as originally planned. It may change the timing, adjust the scope, negotiate different terms, arrange financing, sequence several investments differently, or decide not to proceed at all.

Once the commitment is made, many of those choices narrow.

This is why moving upstream is not simply a financial concept.

It is a management concept.

Consider the large-customer examples we have used throughout the guide. Finance can eventually show management that Receivables have increased and Inventory has grown. Those numbers are useful, but the business had a much greater range of choices while Sales was still negotiating the relationship.

Management could consider the customer's expected volume, price, payment terms, service requirements, Inventory commitment, operating support, and financial capacity together before the relationship became embedded in the company.

The same principle applies to a capital expenditure.

Once equipment has been installed and financing arranged, management's choices are very different from what they were while the investment was still under consideration.

Moving upstream does not guarantee a better result.

It gives management a better opportunity to make a more complete decision.

That is an important distinction because the central idea of this book is not that Finance should become more powerful.

It is that financial consequences should become visible earlier.

## Make Cash Consequences Visible

Most managers do not need to become financial experts.

Salespeople need to understand customers, competitors, markets, and commercial relationships. Purchasing needs to understand suppliers, sourcing, availability, and purchase economics. Operations needs to understand production, service, capacity, quality, and efficiency.

Those areas of expertise should remain where they belong.

The objective is not to make every manager think like a CFO.

It is to give managers enough visibility to understand that important decisions can create financial consequences outside the function where those decisions originate.

A salesperson negotiating a large account does not need to prepare a full cash-flow model. But if the customer wants unusually long payment terms, dedicated Inventory, customized service, and aggressive pricing, the financial implications should be part of the discussion.

Purchasing does not need Finance to approve every order. But when a supplier discount requires a substantial increase in Inventory or a significant advance commitment, the cash consequence deserves visibility alongside the unit-cost savings.

Operations should not avoid carrying appropriate safety stock merely because Inventory uses cash. It should understand the tradeoff being made between service protection and financial capacity.

That is what making cash consequences visible means.

It does not mean cash becomes the only measure of whether a decision is good.

Some of the best business decisions consume substantial cash before creating value. A strong company invests, grows, hires, develops products, adds capability, acquires equipment, serves important customers, and sometimes uses Debt to do those things sooner than internally generated cash would otherwise allow.

The financial question belongs alongside the strategic and operating questions, not above them.

This is where the ten Cash Flow Drivers become useful as a management lens rather than merely financial categories.

Growth.

Pricing.

COGS.

Operating Expenses.

Inventory.

Receivables.

Accounts Payable.

CapEx.

Debt.

Owner Distributions.

Leadership does not need to turn every decision into a ten-driver review.

The value is recognizing that these are places where the consequences of business decisions eventually become visible. When management is considering a significant commitment, the drivers provide a way to think about where those consequences may appear.

Chapter 9 translated that principle into practical questions. What happens to cash? When does it leave and return? What else are we committing to? What has to be true? What happens if we are wrong? What options are we giving up?

Those questions improve visibility.

They do not create certainty.

And that distinction is essential if this way of thinking is going to remain practical in the real world.

## Better Decisions, Not Perfect Decisions

There is no such thing as perfect business decision-making.

A company can evaluate an opportunity carefully, identify the financial consequences, challenge its assumptions, understand the downside, and still end up with a disappointing result.

The future gets a vote.

A customer expected to become a major account may buy less than anticipated. A supplier considered reliable may experience a serious disruption. A product launch may develop more slowly. An employee who appeared exceptionally qualified may not perform as expected.

Equipment may cost more to install.

Interest rates may move.

Economic conditions may change.

A competitor may respond in a way management did not anticipate.

Those possibilities are not failures of the decision philosophy in this book.

They are the realities of business.

The purpose of better decision-making is not to remove uncertainty. It is to improve the quality of the thinking that precedes a commitment and increase management's ability to respond when reality develops differently from the plan.

This distinction matters because outcome and decision quality are not the same thing.

A thoughtful decision can produce a poor outcome.

A careless decision can occasionally produce an excellent one.

If management judges every decision only by the eventual result, the organization can learn the wrong lessons.

Imagine a company that purchases additional Inventory before an anticipated surge in demand. Management has strong customer information, understands the financial commitment, has adequate liquidity, and believes the expected opportunity justifies the investment.

Demand unexpectedly collapses because of an external event nobody could reasonably have anticipated.

The financial result may be painful.

That does not automatically mean the original decision was irresponsible.

Conversely, a manager can make a poorly considered decision that happens to work because market conditions turn out favorably. The positive result does not transform the process into good management.

This is why better decision-making requires a degree of humility.

Management should ask whether the information available at the time was considered appropriately, whether the assumptions were reasonable, whether the financial commitment was understood, and whether the company had sufficient capacity to absorb uncertainty.

Afterward, leadership can compare what was expected with what actually happened and learn from the difference.

That learning becomes increasingly important as a company grows.

In a smaller business, the owner may personally remember why nearly every important decision was made. As decision-making becomes distributed across more people, that institutional memory becomes less reliable.

A strong management organization does not expect people to predict the future perfectly.

It expects them to think clearly, make reasonable decisions with the information available, recognize meaningful financial consequences, and adjust as new information emerges.

That is a much more sustainable standard.

It also reinforces an important point we established early in this guide.

Cash flow is influenced throughout the organization.

But responsibility for ensuring that the enterprise sees those consequences collectively ultimately belongs somewhere.

It belongs to leadership.

## Cash Flow Is Everyone's Result—and Leadership's Responsibility

One of the easiest misunderstandings of the phrase **cash flow is everyone's responsibility** is that every employee should somehow become responsible for managing cash.

That is not what I mean.

Finance has responsibilities that belong to Finance. Accounting has responsibilities that belong to Accounting. Sales, Purchasing, Operations, and other functions each have expertise and decision authority that should remain appropriately distributed.

What everyone shares is influence over the result.

Sales influences Pricing, Growth, customer economics, and Receivables.

Purchasing influences COGS, Inventory, supplier terms, and Accounts Payable.

Operations influences efficiency, capacity, Inventory, quality, and resource requirements.

Management decisions shape Operating Expenses, people, technology, and infrastructure.

Leadership makes decisions about Growth, CapEx, Debt, and strategic commitments.

Owners determine how much cash remains in the business and how much leaves through distributions.

The financial consequence of those decisions eventually converges in the cash the business generates, consumes, retains, borrows, invests, and requires.

That is why cash flow is everyone's result.

Leadership's responsibility is different.

Leadership has to ensure that the enterprise sees enough of those consequences collectively to make sound decisions.

No salesperson sees the entire business.

No purchasing manager does either.

Operations has its perspective.

Finance has another.

Each perspective is incomplete by itself.

Ownership and senior leadership have to create the conditions in which important decisions are viewed across those boundaries when the significance of the commitment warrants it.

That does not require every decision to move upward.

In fact, a growing company becomes stronger when more decisions can be made effectively without the owner's direct involvement.

The leadership objective is not to make all the decisions.

It is to improve the environment in which decisions are made.

Managers should understand what they are responsible for, what information matters, when a decision has consequences outside their function, and when other perspectives need to enter the conversation.

Finance should help make economic consequences visible without becoming an organizational roadblock.

Functional managers should be able to pursue their legitimate objectives without treating those objectives as though they exist independently from the enterprise.

Ownership should be able to establish priorities without becoming the approval bottleneck for every meaningful choice.

That is what decision management begins to look like.

Not bureaucracy.

Not centralized control.

Not financial analysis for its own sake.

It is a business in which important decisions increasingly reflect awareness of the complete enterprise rather than only the objective directly in front of the person making them.

This returns us to the distinction we established in Chapter 3.

Functional optimization matters.

The enterprise still has to win.

And at the executive level, that is where cash-flow management becomes something larger.

It becomes decision management.

Throughout this guide, we have moved progressively upstream. We began with the cash result and asked where it came from. We followed financial numbers back into business decisions, examined the ten primary Cash Flow Drivers, explored how reasonable functional decisions can combine into unintended enterprise consequences, and then considered the questions management can ask before the next commitment is made.

The central idea has remained consistent throughout.

Today's cash flow carries the financial consequences of decisions and circumstances that came before it.

Tomorrow's cash flow is already being shaped by decisions being made today.

Leadership cannot control every circumstance that will influence the result.

But it can improve the visibility surrounding the decisions the company controls.

That is the management opportunity.

And it brings us back to where this guide began: a Sunday afternoon when the financial consequence was already impossible to ignore.

# CONCLUSION

# The Decision Behind Tomorrow's Cash Flow

## The Problem Was Never Just Cash

This guide began with a phone call on Valentine's Day in 1988. I had been in my new CFO position for approximately one week when the Controller called to tell me that we could not make payroll the following Friday. Approximately 300 employees were expecting to be paid, the company did not have enough cash, and available borrowing capacity was essentially exhausted.

At that moment, the problem was undeniably cash. We had five days to find enough of it to make payroll, and nothing in the preceding chapters changes that reality. When a company cannot meet an immediate obligation, leadership has to solve the immediate problem because employees cannot be paid with strategic insight and suppliers cannot deposit better management thinking.

But the phone call was not when the financial condition began. It was when the condition became impossible to ignore.

By that Sunday afternoon, Inventory had already been purchased. Customers had already been sold products at particular prices and under particular terms. Employees had already been hired, Operating Expenses had already been incurred, capital had already been committed, and financing capacity had already been consumed.

Some of those decisions may have been appropriate. Others may have looked different in hindsight, and external circumstances undoubtedly played a role as well. The point was never that one terrible decision caused the crisis.

The point was that the bank balance was showing us the accumulated financial consequence of things that had already happened.

That distinction stayed with me long after we made payroll. Over the decades that followed, as my responsibilities expanded beyond Finance and into broader operating, executive, and entrepreneurial roles, I kept seeing variations of the same pattern.

Cash flow often appeared to be the problem because cash was where the pressure became visible.

The story usually began earlier, with decisions.

## Today's Cash Reflects Yesterday's Decisions

Throughout this guide, we have examined ten primary Cash Flow Drivers: Growth, Pricing, Cost of Goods Sold, Operating Expenses, Inventory, Receivables, Accounts Payable, Capital Expenditures, Debt, and Owner Distributions.

They provide a useful financial structure for understanding where cash is generated, consumed, delayed, borrowed, invested, retained, and distributed. But businesses do not really make decisions called Inventory, Receivables, COGS, or Growth.

They make business decisions.

A customer is pursued, a price is negotiated, a supplier is selected, an order quantity is increased, a production run is scheduled, an employee is hired, payment terms are accepted, equipment is purchased, Debt is incurred, or a distribution is made. Eventually, those choices become visible in the ten drivers.

That is why the numbers matter, but the numbers are not enough.

Inventory tells management how much financial capacity is committed there. It does not fully explain why the Inventory exists. Receivables show how much customers owe the company, but they do not fully explain the customer, pricing, credit, service, and payment-term decisions that created the balance.

Operating Expenses show what the business is spending, but behind that number are decisions about people, technology, facilities, marketing, infrastructure, and capability. Debt shows the financing obligation, but not necessarily the investment, growth, working-capital requirement, or other decision that caused management to borrow.

The financial result provides visibility. Understanding the decisions behind it provides management insight.

That is the shift this guide was designed to create.

When a financial number moves, the first question should not always be how to move it back. Sometimes the better starting point is to ask what decisions created the result management is seeing.

That question moves leadership upstream. It also creates a more important opportunity than simply explaining the past, because the past cannot be changed while tomorrow can still be influenced.

## Today's Decisions Are Creating Tomorrow's Cash Flow

At this moment, decisions are being made throughout your business.

Sales may be negotiating with a customer. Purchasing may be evaluating a supplier proposal. Operations may be deciding how much product to build. Management may be considering another hire. Leadership may be evaluating equipment, technology, capacity, or expansion, while ownership may be deciding how much cash to retain and how much to distribute.

Most of those decisions will not be described internally as cash-flow decisions, and they do not need to be. They are business decisions with financial consequences.

Some of those consequences will appear almost immediately. Others will take weeks, months, or years to become fully visible.

That timing difference is what creates the opportunity.

Yesterday's decisions may already be embedded in today's financial position. Some can still be adjusted, while others cannot. Tomorrow's position is different because many of the decisions shaping it have not yet been finalized.

The price may not yet be agreed to. The Inventory may not yet be ordered. The employee may not yet be hired. The equipment may not yet be purchased. The financing may not yet be arranged, and the distribution may not yet be made.

Management still has choices.

That is why the most important cash-flow question may not be only the retrospective one we have used throughout this guide:

**What decisions created the cash flow we're experiencing today?**

The more valuable companion question is:

**What decisions are we making today that are creating tomorrow's cash flow?**

That question changes when cash-flow management takes place. Instead of waiting for the financial consequence to appear and then asking Finance to explain it, leadership begins considering the consequence while the decision is still being shaped.

That does not mean cash should dominate the decision. It means cash becomes part of the decision.

## Better Decisions Create Stronger Cash Flow

There is an important distinction I want to preserve as we reach the end of this discussion.

Better business decisions do not necessarily produce more cash immediately. A company may make an excellent decision to increase Inventory because customer demand requires it. Management may hire ahead of growth, purchase equipment, enter a new market, accept longer terms from a strategically important customer, or make a substantial investment in technology.

Each decision can reduce near-term financial capacity and still strengthen the business.

Likewise, a decision that improves cash in the short term is not automatically a good decision. A company can increase cash temporarily by postponing necessary maintenance, cutting productive investments, carrying inadequate Inventory, reducing important marketing activity, or refusing opportunities that require working capital.

The bank balance may improve while the enterprise becomes weaker.

That is why better decision-making cannot be defined simply as maximizing cash. It means understanding what the decision requires financially, what management expects in return, what assumptions have to be true, what other commitments the decision creates, and whether the company has the capacity to absorb the consequences if reality develops differently from the plan.

Sometimes that understanding will lead management to commit substantial cash. Sometimes it will lead leadership to change the timing, scope, financing, or terms. In other situations, the answer will be no.

What improves is not necessarily the immediate cash number. What improves is the quality of the decision.

Over time, better decisions made across Growth, Pricing, Costs, Expenses, Working Capital, Investment, Financing, and Owner Capital can create a stronger financial result because the company's resources are being committed more deliberately and with greater visibility.

That is the connection.

Better decisions do not guarantee stronger cash flow because business is too uncertain for guarantees. But better decisions improve the possibility that the cash flow the company eventually experiences is consistent with what management intended to create.

And stronger cash flow can change what becomes possible next.

## Stronger Cash Flow Creates More Options

This is where this guide connects naturally with its companion, *Cash Flow Creates Options*™.

The two books answer different questions. This guide asks where cash flow comes from, and the answer is that much of it emerges from decisions made throughout the business. *Cash Flow Creates Options*™ asks why stronger cash flow matters beyond the number itself.

The answer is that stronger financial capacity can expand the choices available to the business and ultimately to the owner. That relationship is the larger BusinessWiser™ philosophy reflected in the progression established in the blueprint.

Better business decisions can contribute to stronger cash flow. Stronger cash flow can create more options. Those options can help management build a more successful business, strengthen owner wealth, and create greater flexibility around the role the business plays in the owner's life.

That does not happen automatically. Better decisions do not guarantee success, stronger cash flow does not guarantee wealth, and greater financial capacity cannot define a better quality of life for another person.

What stronger financial capacity can provide is greater ability to choose.

The business may be able to invest when an attractive opportunity appears instead of watching it pass. Management may be able to grow deliberately rather than stretching every available resource. The company may be able to reduce Debt, withstand uncertainty, hire stronger people, improve systems, or wait for a better opportunity.

Ownership may eventually have greater freedom to diversify wealth, change roles, reduce involvement, pursue another opportunity, or simply continue building the company from a position of greater financial strength.

That is why cash flow ultimately matters.

But this guide began one step earlier.

Before stronger cash flow can create more options, management has to understand where cash flow comes from. It comes from the business, and much of the business is shaped one decision at a time.

## The Decision Comes First

If there is one idea I hope remains after the details of this guide fade, it is that when you see a cash-flow result, you should look behind it and ask what decisions created it.

Not because someone necessarily made a mistake. Not because every unfavorable financial result can be prevented. And not because every decision should be made primarily to protect cash.

The reason is more practical: understanding the decisions gives leadership somewhere to act.

A bank balance is a result. A receivable is a result. Inventory is a result of many decisions and circumstances. Margins reflect decisions and conditions that developed before the percentage appeared on a report, and Debt usually exists because something caused the company to need or choose financing.

The numbers matter enormously, but they appear downstream.

The management opportunity exists upstream.

Sales can consider the complete economics of an important customer before the terms are finalized. Purchasing can consider financial capacity alongside unit economics before the order is placed. Operations can balance availability, efficiency, and cash commitment before additional Inventory becomes embedded in the business.

Leadership can consider the timing and secondary requirements of growth before the organization is fully committed. Ownership can consider distributions alongside the financial needs and opportunities of the enterprise, while Finance can help make those consequences visible while management still has choices.

None of this requires perfect foresight. It requires a broader field of vision.

Nearly forty years ago, I received a phone call telling me we could not make payroll. By the time the phone rang, the financial consequence was already there.

Today, I would still respond to that immediate problem the same way: find the cash and make payroll.

But once the immediate pressure was behind us, I would ask the question that became much more important over the rest of my career:

**What decisions created the cash flow we are experiencing?**

Then I would turn the question forward:

**What decisions are we making today that are creating the cash flow we will experience tomorrow?**

That is where the opportunity lies, because cash flow may be where the results become visible, **but the decisions come first.**

# Where Better Decisions Lead

If this Executive Guide accomplished what I hoped it would, the next time you look at your company's cash flow, you'll look beyond the number and consider the decisions that helped create it.

Growth. Pricing. Costs. Expenses. Inventory. Receivables. Payables. Capital expenditures. Debt. Owner distributions.

Those decisions are made throughout the enterprise, and their financial consequences eventually become visible in cash flow.

That leads naturally to another question:

**Why does stronger cash flow ultimately matter?**

That's the subject of the companion BusinessWiser™ Executive Guide:

**Cash Flow Creates Options™**

*Why the Ultimate Value of Cash Flow Is the Choices It Creates*

Because the ultimate objective isn't simply to produce more cash. It's to create greater financial capacity—and with it, more options for the business and its owner.

The two guides complete a natural progression:

**Better Decisions → Stronger Cash Flow → More Options**

# From Better Thinking to Disciplined Execution

Understanding the relationship between decisions, cash flow, and options is an important first step. But lasting improvement requires more than understanding. It requires turning better thinking into disciplined execution.

That's why I created the **BusinessWiser™ Cash Flow Mastery System**.

The BusinessWiser™ Cash Flow Mastery System is built around six integrated frameworks, each addressing a different aspect of business performance. Together, they create a practical operating system designed specifically for owner-led product businesses.

### CASHFLOwiser™

See the structural truth behind growth, profitability, working capital, and cash flow.

### DRIVERwiser™

Focus improvement on the operational drivers that have the greatest impact on cash flow.

### FORECASTwiser™

Replace uncertainty with annual, quarterly, weekly, and daily financial visibility.

### PLANwiser™

Translate strategy into disciplined quarterly execution.

### CULTUREwiser™

Build a culture where better financial decisions become part of everyday operations.

### VALUEwiser™

Convert stronger cash flow into greater business value, owner wealth, and long-term business success.

Each framework delivers value independently.

Together, they help create something every owner wants:

A business that's stronger.

More predictable.

More valuable.

And filled with more options for the future.

## Built for Real-World SMBs

BusinessWiser™ was designed specifically for owner-led product businesses where time, money, and manpower are always limited.

Everything follows the same philosophy:

**See clearly.**

**Decide deliberately.**

**Execute consistently.**

Because better decisions strengthen cash flow.

And stronger cash flow creates more options.

# When You're Ready

This Executive Guide introduced one important idea. The BusinessWiser™ Cash Flow Mastery System provides the practical frameworks, tools, and guidance to help your team put that thinking into practice.

The complete system brings together financial analysis, forecasting, planning, reporting, and execution resources designed for owner-led product businesses. Your management team applies the tools. You oversee priorities, progress, and results.

To make these resources more accessible, I'm offering the complete system for **$490 for a limited time—a $500 savings from the regular $990 price.**

**One-time purchase. No recurring system fee.**

If you're ready to build greater financial visibility and a more disciplined approach to business decisions, I invite you to explore the system and its free preview.

**Explore the Cash Flow Mastery System**

Better decisions can strengthen cash flow. Stronger cash flow can expand what your business makes possible.

**Cash Flow Creates Options™.**

## Implementation Note

The concepts in this executive guide are designed to improve clarity and decision-making within owner-led businesses. Every company operates under unique conditions, and results will vary based on execution quality, market environment, and management discipline.

Before implementing material financial or operational changes, consider consulting qualified advisors who understand your specific circumstances.

Sustainable improvement comes from disciplined application over time.