The Implications of Imperfect Cash Flow Management in Business

* Fazni Mohamad Fadzillah[1], Azura Mohd Noor[1], Norizam Ahmad @ Muhammad[1]

[1]Faculty of Accountancy, Universiti Teknologi MARA Cawangan Perlis
*Corresponding author: faznimf @uitm.edu.my

Cash Flow is essentially the inflow and outflow of money from a business. Abdullah et al. (2021) in their study defined 'Cash Flow' as the addition or reduction of cash based on receipt and payment of cash in a business. Moreover, cash flow is the amount of funds received or paid by the organization during the reporting or accounting period. In addition, Lazar (2018) explained that cash flow is the cycle of cash inflows such as sales, cash collected from customers, and investments and cash outflows such as payments for purchases, payments to suppliers, salaries, raw materials, and so on. Cash flow is a vital indication of your business's overall financial strength.

Positive cash flows (inflow) reflect the receipt of funds in the organization, which means the business is successively efficient. While negative cash flow on the other hand, represents the outflow or expenditure of funds by the business. If the business spends more than it earns, this could lead to problems paying bills, employees' salaries, and wages, or even hinder the ability to take advantage of new business opportunities. This article discusses the implication of imperfect management of cash flow on a business.

Cash flow management is a very significant aspect of business to ensure smooth business transactions. If this cash flow management is carried out efficiently, a good relationship will be built with the parties who are interested in business affairs, for example a good relationship with the supplier when the business is able to pay the debt in the specified time. According to Galai et al. (2016), cash flow management is a financial tool that aids in the achievement of any commercial enterprise's primary purpose, which is to make a profit. The fundamental purpose of cash flow management in a business is to determine the degree of financial sufficiency, maximize funds, and use them efficiently.

Various strategies have been identified and implemented in Malaysia's post-Covid 19 economic recovery efforts. This includes efforts to restore micro, small and medium enterprises (PMKS) because this group is considered to be the driver of domestic investment development in Malaysia. Despite this in achieving recovery, PMKS is now seen to be facing cash flow problems after about two years of not being able to operate fully and many admit to lacking capital to return their respective businesses to their pre-pandemic levels (Kosmo, 3 November 2022). This is also supported by a statement from the Ministry of Entrepreneur Development and Cooperatives (MEDAC) which states that the main challenge for entrepreneurs is cash flow constraints as well as the number of sales that have decreased during the implementation of the Movement Control Order (MCO) (Metro, 18 January 2022).

The integrity and cash worthiness of the business will not be disputed among the industry players. However, with the world economy still in the recovery stage from the Covid 19 pandemic, many businesses are facing cash flow management problems. The daily operations of the business will be affected, and it is possible that the business will go bankrupt due to inefficient cash management. Horne & Wachowicz (2008) said that cash flow provides important information to identify the ability to generate cash, the quality of net profit, the trend of investment as well as the need to mobilize external sources of funds, debt repayment capacity, the ability to distribute interests to owners, the ability to be independent. finance, and many other financial issues.

Among the implications of imperfect cash flow management for a business is the lack of merchandise. This happens when there is a lack of cash flow or stagnant cash flow. This makes it difficult for businesses to add merchandise because there is not enough money for cash purchases or payment of credit transactions to suppliers when payment time comes. Egwu et al. (2021) found that cash flow management significantly influence the meeting of financial obligations. Business that effectively manage their cash flow have the tendency of meeting their financial obligations. There is a need for owner to effectively track the inflow and outflow of cash in their business as this contribute to the successful of the business.

The next implication is when the owner fails to explain business-related expenses such as the purchase of office materials, employee wages, various types of bills and so on. If the expenses of daily affairs cannot be met, then it will affect the smoothness of the business operations. For instance, employees who do not receive their wages or salaries will protest or are not motivated to work harder. This will lead to decrease in business productivity and reputation of the business will also be affected.

In the worst-case situation, persistent cash flow problems can drive a business toward insolvency and financial instability. Without sufficient funds to cover operational expenses and debts, the business may be forced to go into liquidation, leading to significant financial losses for stakeholders. When workers lose their jobs and income, it will greatly impact the country's economic level.

Sufficient cash flow allows a business to manage expenses perfectly. But if it happens otherwise, it will hinder the business operations. Imperfect cash flow management will also cause the business to be unviable, the level of indebtedness will increase and even the level of profit will also decrease. If this implication continues the reputation of the business will be at its lowest level. Investors will have difficulty trusting the ability of businesses to manage their cash flow and this will cause investors to turn away and invest in other competitors. When investors lose trust in a business, efforts to restore that trust are very difficult and take a long time.

In conclusion, cash flow is critical factor to a success of a business. It represents the lifeline of every business. When a business fails for financial reasons, this may be traced to insufficient cash flow or lack of effective management. Due to that, a business should take early steps so that the cash flow of the business is at an optimal level. This includes regularly forecasting cash flow to anticipate and prepare for potential shortfalls, optimizing inventory management to reduce unnecessary costs, and negotiating favourable payment terms with suppliers and customers. If this matter is taken for granted and not managed perfectly, then more serious implications may hit the business. In fact, it is feared that the business performance will be worse, causing a business to go out of business because it is unable to manage cash flow wisely.

REFERENCES

Abdullah, H., Sarpin, N., Omar, R., Mohamed, S., & Ismayatim, N. (2021). Kajian masalah kewangan yang dihadapi kontraktor bumiputera semasa fasa pembinaan. *Research in Management of Technology and Business, 2*(1), 812-830.

Egwu, E. M., Orugun, F. I., & Adelakun, A. (2021). Exploration of cash flow management for enterprise's business performance. *Asian Journal of Economics, Business and Accounting*, *21*(10), 97-105.

Galai, D., Hillel, L., & Wiener, D. (2016) *How to create a successful business plan: For entrepreneurs, scientists, managers, and students.* New Jersey: World Scientific.

Horne, J. C. V., & Wachowicz, J. M. (2008). *Fundamentals of financial management* (13th edition) Prentice Hall.

Lazar, J. (2018). *Company & group financial reporting.* (9th edition) Pearson.

Muhammad Ikhwan, I. (3 November 2022). *MPN prihatin isu aliran tunai yang dihadapi PMKS.* https://www.kosmo.com.my/2022/11/03/mpn-prihatin-isu-aliran-tunai-yang-dihadapi-pmks/

Sri Ayu Kartika, A. (18 Januari 2021). *Kekangan aliran tunai.* https://www.hmetro.com.my/bisnes/2021/01/665355/kekangan-aliran-tunai.