



7 WAYS TO IMPROVE LIQUIDITY

By Pam Newman

Find out how to calculate your company's liquidity ratio and how to improve it.

Liquidity is your company's ability to pay the bills as they come due. We've all heard the saying 'Cash is king,' so here are seven quick and easy ways to improve your company's liquidity.

1. **Sweep accounts:** Use sweep accounts through your financial institution. This will allow you to earn interest on any excess cash balances by 'sweeping' or transferring the funds into an interest-bearing account when the funds aren't needed and sweeping them back to your operating account when you do need them.
2. **Overhead:** Assess your overhead costs and see if there are opportunities to decrease them. Lowering overhead has a direct impact on profitability. Overhead expenses, including rent, advertising, indirect labour and professional fees, are indirect expenses that you incur to operate the business outside of direct material and direct labour.
3. **Unproductive assets:** If you have unproductive assets that the business is just storing, then it's time to get rid of them. The only reason you should spend money on assets such as buildings, equipment and vehicles is to generate revenue.
4. **Accounts receivable:** Monitor accounts receivable effectively to ensure that you're billing your clients properly and that you're receiving prompt payments.
5. **Accounts payable:** Negotiate longer payment terms with your vendors whenever possible to keep your money longer.
6. **Owner's draws:** Monitor the amount of money that's being taken out of the business for non-business purposes such as owner's draws. Taking too much money out can put an unnecessary cash drain on the business.
7. **Profitability:** Review the profitability of your various products and services. Assess where prices can be increased on a regular basis to maintain or increase profitability. As your costs increase and markets change, prices may need to be adjusted as well.

Implement these seven easy tips in your business to improve your liquidity. It will help to ensure that you have the proper cash flow levels for continued operations and company growth. There are two main financial ratios used to measure a company's liquidity ratio:

- Current ratio equals current assets divided by current liabilities. This should have a target ratio of 2 to 3, which indicates that you have adequate liquid funds to pay your current obligations.
- Quick ratio equals current assets (less inventory) divided by current liabilities. This should have a target ratio of 1 to 2, which indicates your liquid funds without selling your inventory.

You can find the balances of your current assets and current liabilities on your balance sheet. Speak to your accountant if you need further guidance and analysis. Looking at industry information also can help you assess how you compare to others in your specific industry.

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