

Determining Vitamin C Deficiency: and An Important Question To Be Asked

by Ken Young C.C.P. Emeritus.

Those who have been trained in the art of credit management know very well the 5 C's of credit that should be investigated prior to granting a line of credit. These "C's" consist of the following:

- 1) Capacity measures the borrower's ability to repay the funds by assessing the cash flow and financial capabilities of the company. Investigating the trade references of the firm gives insight into the past history and current status of repayment of amounts owing, and is a good method to help determine the probability of timely repayment.
- 2) Capital refers to the investment made into the company. A large investment into the firm decreases the chance of default. An element of excess capital provides a cushion for any unexpected financial setback. The questions that need to be asked are: Who is investing more in the firm, the owner or the lender? And if the firm is losing money how long can it survive?
- 3) Collateral determines what security the firm has available, and what has already been pledged. Has the firm granted the bank collateral on all of the assets?

Is it appropriate for you to consider an element of security from the firm or a personal guarantee? This gives the supplier a "plan B" if everything does not go well.

- 4) Conditions relate to a number of areas, such as interest rate or currency fluctuation and the life cycle or shelf life of the product. If the firm is barely making ends meet could they withstand an increase in the interest rate? Is there new technology that is going to make their product irrelevant soon? Is the shelf life almost at the end? If the firm exports and sells in a different currency what effect could that have? Will a change in the overall economic conditions have an effect on the buying patterns of the customer?
- 5) Character gauges the trustworthiness of the owner(s). Do you feel comfortable selling to them? Do you perceive them to be honest, possess a sense of responsibility and believe that they will keep their word if they make a commitment? This may be described as a "gut feel."

I recall very clearly many years ago at an industry trade meeting, a fellow Credit Manager made a unique point about financial statements. He said that when you are reviewing financial statements (which assists greatly in the assessment of the 5C's) with a customer, the first thing you should do is to ask, "Is there anything you would like to tell me about these before I review them?"

This gives the client the golden opportunity to explain any weak areas and to let you know what they are doing to remedy them. If they don't disclose anything specific at the time and upon review of the statements you ultimately see some areas of concern, before

you ask for an explanation from them about it, you may ask yourself are they even aware of this? Is there a concern that the firm is suffering from a Vitamin C deficiency – namely, cash, credit and customers? That's a very simplified version of the 5C's.

Over the years I've found that asking this question can get to the heart of concerns more quickly. This allows for more time to be spent on questioning how the business will change and grow profitably in the future and on determining how your firm can assist that.

Ken Young C.C.P., C.C.P. Emeritus

Ken has been a credit management professional for over twenty-five years and has global experience in a broad range of industries including the food (aquaculture and beverage), chemical, manufacturing and transportation sectors. Most recently he was the Credit & Collection Manager at Pepsi Bottling Group in Canada.

Ken has delivered a successful series of keynote addresses on credit in Kingston and Montego Bay Jamaica. He was also a part of a small team that designed and implemented enhanced strategies for the collections department of a large firm in Indonesia. He serves on the board of the Credit Institute of Canada as well as the National Credit & Financial Executives Forum.

You can contact Ken at Young.Ken@hotmail.com