

CASH ASLEEP IN THE BUILDING · CHAPTER FIVE

The Payment Run Held Until Monday

Four ways a day of cash can move, and why only one of them is a gain.

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A NOTE BEFORE YOU READ

This work is offered for education and leadership development. It is not legal, financial, accounting, investment, medical or psychological advice; take the advice of a qualified professional who knows your circumstances. Companies and events are described from the public record as the author understands it; characterisations are the author's analysis. Examples are illustrative, and no particular outcome is promised to any reader.

ABSTRACT

Four ways a day of cash can move, and why only one of them is a gain. It is ten to five on the last Friday of the quarter, and the payments clerk has the supplier run on her screen, approved and ready. Two hundred and twelve invoices, every one of them due, every one of them checked. At four o'clock the group's finance office rang her manager, and her manager has just come over to her desk, a little embarrassed, to say that the run should be held until Monday. Nothing is wrong with it. The group would simply like the quarter's closing cash balance to be higher, and three days will do that. The suppliers will be paid on Monday morning. Most of them will not notice. She holds the run. She knows several of the suppliers will notice, because she is the person they ring, and she knows which ones have payrolls on Monday. Her stomach is tight in the way it gets when she has been asked to do something that is allowed and not right. She logs off at half past five.

CHAPTER FIVE

The Payment Run Held Until Monday

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The Payment Run Held Until Monday

HAUTE LUMIÈRE · CASH ASLEEP IN THE BUILDING · CHAPTER FIVE

Ten to five, the last Friday of the quarter

It is ten to five on the last Friday of the quarter, and the payments clerk has the supplier run on her screen, approved and ready. Two hundred and twelve invoices, every one of them due, every one of them checked. At four o'clock the group's finance office rang her manager, and her manager has just come over to her desk, a little embarrassed, to say that the run should be held until Monday. Nothing is wrong with it. The group would simply like the quarter's closing cash balance to be higher, and three days will do that. The suppliers will be paid on Monday morning. Most of them will not notice.

She holds the run. She knows several of the suppliers will notice, because she is the person they ring, and she knows which ones have payrolls on Monday. Her stomach is tight in the way it gets when she has been asked to do something that is allowed and not right. She logs off at half past five.

She is a composite, drawn from the way quarter-ends are described by people who work through them and in the house's own practice, and no firm is meant. On Monday the group's report will show a stronger cash position and a longer payables period. On Tuesday both will be what they were on Thursday.

Ammanuel Santa Anna's book on organisational silence lists the ways an organisation spends energy keeping up appearances it knows to be incomplete, and the first item on the list describes the closing balance exactly: "Crafting messages that are technically accurate but strategically misleading".[34]

This chapter makes one claim, and it closes the argument of the four before it. A day of cash released from a business is worth sharing only if it can be told apart from a day moved in time, moved to someone else, or borrowed; and that can be done only by measuring the cycle as an average over time, by sorting every day by where it came from, and by setting beside it the measures that would show if it had been bought at someone else's expense.

Numbers that can be made

The managing director in Chapter 1 learned to read the cash conversion cycle as a map of who holds the money. Its weakness as a map is that it is usually drawn on one night: the last day of a quarter or a year, when the balances are taken. Anything that changes the balances on that night changes the map, whether or not it changes the business.

The accounting literature has studied this for a long time, under the name of earnings management, and one strand of it is directly about working capital. In 2006 Sugata Roychowdhury published evidence that managers of American firms take real operating decisions, not only accounting ones, in order to avoid reporting an annual loss.[35] The decisions he studied included price discounts to bring sales forward, overproduction to spread fixed costs over more units and so lower the reported cost of each, and cuts to discretionary spending. Two of those three act directly on the cash cycle. Discounted, accelerated sales arrive with receivables attached, often on easier terms. Overproduction is stock. A firm can, in other words, make its profit look better this year by making its working capital worse, and the reverse is possible too.

The studies of fiscal year-ends point the same way. Paul Oyer found in 1998 that American manufacturers' sales were higher at the end of the fiscal year and lower at the start, a pattern consistent with salespeople and executives paid on annual thresholds pulling customers' purchases forward.[36] The receivables that a year-end push creates, agreed in a sales office in the last week of a period, as Chapter 3 found, are on the balance sheet on the one night the cycle is measured. The stock that the push draws down is off it. Neither tells a reader what an ordinary week looks like.

A word on the strength of this evidence. These are studies of large listed firms, using public accounts, and they find patterns consistent with deliberate timing; they cannot see into any one firm's intentions, and most firms in their samples are doing nothing of the kind. The point for a leader is not that her colleagues are manipulating the numbers. It is that the numbers can be moved by timing alone, honestly and with permission, as the payments clerk's run was, and that a measure which cannot tell timing from improvement will reward timing.

Santa Anna's canon on value streams has a sentence for the confusion that results, in a passage about what gets measured in an organisation and why: "Measurability is a property of our instruments, not a property of reality." The cash conversion cycle on the last night of a quarter is a property of the instrument.

Four ways a day can move

It helps to be exact about the different things that can shorten a cash cycle, because only one of them is the gain this book has been looking for.

The first is a change in the business. Fewer hoods sit on the floor because the planner and the sales director walked the oldest shelves in Chapter 2 and stopped holding stock against fears that had passed. Invoices are paid on day thirty because the order desk now takes the purchase-order number on the first call. These days are released from the firm's own building, by its own people, and they stay released for as long as the behaviour holds. They are the gain.

The second is a change in terms. Customers are moved from sixty days to thirty, or suppliers from thirty to ninety. The days are real, in the sense that cash really arrives sooner or leaves later, but they are taken from someone else's building. Chapter 4 read the research on what the second kind costs a supplier, and it is not small. A shortened customer term may be entirely fair, if the old term was a gift nobody had decided to give. A lengthened supplier term is, in most of the cases the research describes, a loan from the weaker party.

The third is financing. A firm sells its receivables to a factor, or its suppliers are paid early by a bank through a programme while the firm pays the bank later. The cycle shortens on paper. The firm is still financing its trade; it has moved the cost to a different line. This is the kind of day that the accounting standard-setters moved to make visible, in America in 2022 and internationally in 2023, by requiring buyers to disclose their supplier finance programmes, so that a reader can see what part of a firm's payables is, in substance, money it has borrowed.[37]

The fourth is timing. The payment run is held until Monday. The stock count is taken after a large shipment and before the next delivery. The days exist for one night. They are not a gain of any kind, and they cost the suppliers whose payment slipped, and the trust of the clerk who held it.

A measure worth signing sorts every day into one of these four, and counts only the first as found. The second is counted separately and examined, because it may be fair or it may be extraction. The third is shown, and not counted. The fourth is removed. None of this needs software. It needs someone to ask, of each change in the number, where the day came from.



How short is too short

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How short is too short

There is a second discipline, and it guards against the opposite error: the firm that believes every day removed is a day gained, and keeps removing them.

The research read in the earlier chapters says plainly that this is not so. Hong Chen, Murray Frank and Owen Wu, studying American manufacturers from 1981 to 2000, found that firms with abnormally high inventories had poor long-term stock returns, and firms with slightly lower than average inventories did well, but "firms with the lowest inventories have only ordinary returns."[38] Nihat Aktas, Ettore Croci and Dimitris Petmezas, studying American firms from 1982 to 2011, found evidence of an optimal level of working capital, and that firms moving towards it from either direction tended to improve their performance.[39] Both are associations across many firms, and neither sets a target for any one. Together they say that a cycle can be too short, and that the cost of too short is paid somewhere the cycle does not look: in orders lost for want of stock, in customers who move to a supplier that offers terms, in a factory that stops while a part is rushed in.

So the measure needs companions. Beside the days of stock, the share of orders shipped complete and on time, so that a fall in stock that is really a fall in service shows at once. Beside the days of receivables, the number of customer complaints and lost accounts, so that terms tightened past what customers will bear are visible before the sales figures show it. Beside the days of payables, the share of supplier invoices paid on the agreed date, and the number of suppliers asking for early payment, so that a lengthening that is really a delay is named as one. The house's first business book argued that a measure that pays people should almost never travel alone, because a lonely metric can always be accused of gaming. A working-capital figure is the loneliest metric in a firm.

The Luminous 100, the house's reading of the frameworks every consultancy sells, frames the same idea in its entry on systems thinking, where it asks of any measured system a question that turns the search for faults into a search for what already works: "Where are the virtuous cycles already alive in this system?" A good working-capital measure finds them: the department whose days have fallen and whose service has held, which is the behaviour to copy.

A number made in the light

Santa Anna's canon has a passage on what it calls shadow in governance, and one of the costs it names is the decision that looks like a decision and is not. "Shadow governance produces decisions that look like decisions but lack the genuine collective commitment that makes decisions effective." A closing balance improved by a held payment run is a number of that kind. Everyone who made it knows how it was made, and nobody believes it, and the next quarter has to be made the same way.

His writing on money describes the inner side of the same habit. "Money that is attended to with anxiety contracts," he writes. "Money that is attended to with avoidance stagnates." A group that holds its payment run every quarter-end is attending to its money with anxiety, about how one number will look on one night, and the contraction lands on the suppliers and on the clerk.

There is a better way to hold the number, and it is less dramatic than it sounds. Measure the cycle as an average over the year, from monthly balances, so that no single night decides it. Show it as a line, month by month, with the range of the last two years drawn behind it, so that a good month is read against ordinary variation before anyone celebrates it, as the finance director in Where the Flow Stops learned to read her scrap rate. Adjust for what moves the number for reasons nobody inside controls: a change in the mix of customers, a season, a rise in steel prices that makes the same stock worth more. Name those adjustments in advance. And sort every change into the four kinds above, in a ledger anyone in the firm can read.

That ledger is the practice this chapter is about. It is not a report for the board, though the board may read it. It is a record, kept monthly, of every day that has moved in the cycle, with a line for each: what moved it, which of the four kinds it is, which department's behaviour produced it, and what the companion measure did in the same month. A day of stock released by the shelf walk goes in as a change in the business, against the warehouse and the sales office, with service levels beside it. A day of payables added by a supplier who agreed to a change goes in as a change in terms, with a note of what the supplier was told. A day borrowed through a programme goes in as financing. A day made by a held payment run goes in as timing, and comes out again the following week.

The ledger has one more virtue, and it is the one the payments clerk would notice first. It gives a place to the knowledge of the people who see the timing happen. The clerk knows which runs were held and which suppliers rang. The warehouse supervisor knows that the stock count was taken the morning after the largest shipment of the quarter. The credit controller knows that three customers were persuaded to pay before the close and will pay correspondingly late in the month after. None of this is secret, and none of it reaches a board report, because there is no column for it. A ledger that asks, of every movement, what kind it was, is a ledger that has to ask these people, and in asking them it collects what the house's first business book called the knowledge of the person who already knows: paid for once, and until now collected never.

It also changes the conversation between finance and the operating teams. Before the ledger, a cycle that lengthened in a quarter produced a request from the group to bring it down by the next close, and the operating teams, sensibly, reached for whatever would move it fastest. After it, a lengthening produces a question: which kind of day moved, and where? Sometimes the answer is a season, or a large new customer on standard terms, and nothing needs to be done. Sometimes it is a shelf that has started to fill again, and the planner already knows why. The question is cheaper than the request, and its answers are better.



The ledger at quarter-end

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The ledger at quarter-end

Picture the group's finance director, the one who rang the payments manager at four o'clock, a year after she first saw the ledger. She is the person who asked for it, because she had grown tired of a closing balance she could not explain to her own board. Her first instinct had been to dislike what it showed. Of the eleven days by which the group's cycle had improved over the previous year, four were changes in the business, five were longer supplier terms, and two were timing. The improvement she had reported was mostly borrowed.

The second year looks different. She agrees with the operating companies, before the year begins, what the ledger will count, which records it will read and what adjustments it will make, and she writes it on one page and has it signed. The operating companies walk their shelves and their disputed invoices. The supplier terms are left alone, and the payment date is kept. And she tells her own treasury team, in writing, that no payment run will be held for a reporting date, because a held run will go in the ledger as timing and come out again, so there is no longer any reason to hold one.

The cycle improves by six days that year, less than the eleven. All six are changes in the business, and all six are still there in the first month of the following year. On-time delivery has not fallen. Supplier invoices are paid on the agreed date. The six days are the first number in the group's working capital that every operating company believes, because each company can find its own share in the ledger and name the people who produced it.

This is where the series meets the question that runs underneath all five chapters. A gain found in a firm's own building, in its stock and its invoices, belongs to the people and the process that produced it, and if it is to be shared with them, or with anyone who helped find it, it has to be measured first in a way both sides believe. The ledger is how that measurement is made for cash. It does not settle how such a gain is divided, which depends on the organisation and the people it covers, and this book does not describe it. What the ledger does is make that later decision honest, by producing a figure that is the firm's own, sorted by its source, and agreed before anyone knew what it would say.

There are predictable ways for this to go wrong. A ledger kept by treasury alone becomes treasury's defence, and the operating companies stop reading it. Adjustments agreed after the results are in will be read, correctly, as the side that lost trying to win. And a ledger that counts the second kind of day as gain, because the terms were legally agreed, will slowly fill with supplier money and empty of behaviour. Chapter 7 carries the ledger as a working page, with its four columns, the companion measures and the one-page agreement, and Chapter 6 places it in the order of a first ninety days.

Santa Anna's *Ecstatic Economics* states the principle that sits under every line of it: "Money is not neutral. It is a design system, and the design shapes the behavior." A measure of cash is a design too. Designed on one night, it produces payment runs held until Monday. Designed as an average, sorted by source and set beside its companions, it produces shelves walked and invoices put right, because those are the only things that move it.

Keeping the release ledger

The release ledger is a modest document with a large effect, and the finer points are about keeping it honest when it is inconvenient.

Agree it before the work begins. As with the measurement conversation in *Where the Flow Stops*, almost all of the ledger's credibility is earned before anyone knows what it will show. Decide, on one page, which records it will read, over what period, which adjustments it will make and how, which companion measures sit beside it, and who keeps it. Sign the page with the people whose departments will appear in it. An adjustment proposed after the results are known will be read, correctly, as the side that lost trying to win.

Measure on an average, not on a night. Take the balances of stock, receivables and payables at the end of every month, and compute the cycle as a rolling average over the last twelve or thirteen months. A rolling average cannot be moved by a held payment run or a well-timed shipment, because one night is one point among many. Report the month-end figure too, if the board needs it, but count the release only on the average.

Draw the ordinary range behind it. Plot the monthly cycle against its own history over two years where the records allow, and treat a month as news only when it falls outside that history's ordinary range, or when several months in a row move the same way. Shewhart's chart, read in *Where the Flow Stops*, is the oldest tool for this. One good month is not yet a release.

Name the adjustments in advance. Some things move the cycle that nobody inside the firm controls: a change in the mix of customers, a season, a rise in the price of materials that makes the same stock worth more, a large new customer on standard terms. For each that is likely, agree whether it will be adjusted for, from which record, and how. Keep the list short. Every adjustment is a place where judgment enters, and judgment should enter in the spring, not at the close.

Sort every movement into one of four kinds. A change in the business: stock or receivables reduced by a change in how the work is done. A change in terms: customers or suppliers moved to different terms. Financing: receivables sold, or suppliers paid through a programme. Timing: anything that exists only around a reporting date. Count the first as released. Show the second separately, with a line on what the other party gains. Show the third, and do not count it. Remove the fourth.

Name the department behind each released day. A day released from stock belongs to the warehouse, production and sales who walked the shelves; a day released from receivables to the order desk, warehouse and billing team who put the invoices right. Writing the names in the ledger is what turns it from finance's document into everyone's, and it is what the people who did the work will look for first.

Set the companions beside every line. On-time and complete delivery beside stock. Complaints, lost accounts and the share of invoices right the first time beside receivables. The share of supplier invoices paid on the agreed date, and requests for early payment, beside payables. If a released day comes with a companion moving the wrong way, it is not yet a release; it is a cost moved somewhere the cycle does not look.

Give the keeping to someone the ledger does not judge. The person who keeps it should not be measured on the number it produces. In a group, that may be a management accountant outside treasury; in a smal-

ler firm, someone in finance who reports to the managing director rather than to the department whose days move most. Whoever it is, the departments named in it should be able to check every line against their own records.

Write the no-held-run rule down. A sentence in the agreement: no payment to a supplier will be held for a reporting date, and any that is will go in the ledger as timing. Once that sentence exists, there is no longer any reason to hold one.

Say what it does not settle. The ledger produces a figure that both sides can believe: the cash released from the firm's own building, by its own people, sorted by source. It does not settle how such a gain is shared with the people who produced it, or with anyone who helped find it: the proportions, the timing, the thresholds and the terms. Those depend on the organisation and the people it covers, they are decided with them, and this book does not describe them.

Chapter 6 places the ledger agreement on the tenth day of the first ninety and the first full reading of it at day ninety, and Chapter 7 carries the ledger page, the four kinds, the companion measures and the one-page agreement.

Ten to five, a year later

It is ten to five on the last Friday of the quarter, and the payments clerk has the supplier run on her screen, approved and ready. Two hundred and eighteen invoices, every one due, every one checked.

Her manager walks past her desk on the way to a meeting and does not stop. At five o'clock the run goes, as it was always going to.

On Monday morning nobody rings her. She has time to read the ledger, which the finance office now sends round each month, and finds, near the bottom, a line about the suppliers paid on the agreed date. It says all of them.

A NOTE FROM THE HOUSE

A release ledger is the instrument a gainshare stands on: a day of cash counted in the light, from records both sides already trust, and kept apart from the three kinds of day that are not a gain. Luminous Prosperity Inc. keeps that ledger beside a firm, and is paid as a share of the gain it helps release.

REQUEST A CONVERSATION

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