Back to Basics: Four Key Metrics Your Credit Department Should Consider Tracking

“You can’t improve what you don’t measure,” said Amber Tallmadge, CCE, corporate credit manager at Central States Manufacturing during a 2014 Credit Congress session. It’s a hard point to assail. After all, how is a credit manager to identify what improvements their department needs without hard statistics to back up the assessment? Significant shifts in credit policies, procedures or day-to-day actions should not be based only on feel or anecdotal evidence. The following are a few metrics that every credit professional can gain something from tracking:

Days Sales Outstanding: Though DSO can be out of context, the reality is upper management and finance officers want this number above all others. It is easy to understand, easy to calculate and it is the most used metric by an expansive margin. Yes, it can lead to distortions, but it’s a credit professional’s job to explain what about the numbers doesn’t represent reality. In addition, because it is used by just about everyone, a credit manager can externally benchmark DSO against those of other companies in their industry. Even if DSO is by no means a perfect measure, if your DSO is significantly higher than those in your industry, it could be a red flag.

Average Days Beyond Terms: Some find this to be an easy go-to to present in chorus with DSO. It is a weighted average that essentially tracks if and by how much a customer typically pays late. Having this can help spot seasonal and recurring shifts that happen throughout the year. An important point to remember is if your portfolio contains one or two accounts that are significantly larger than the rest the portfolio’s average can be distorted.

Percent of Invoices Past Due Segmented into 30-, 60- and 90-Day Buckets: There is a big difference between actionable past due amounts and those where the customer’s tardiness isn’t a problem. Obviously, the hope is the largest percentage of past due accounts land in the 30-days or fewer bucket. If the largest total, however, is in the 60+-day or 90+-day bucket, there’s a serious issue with that credit line, one that could dangerously impact cash flow. As the buckets are reviewed, there are also key differences to the action taken. The credit manager is not likely to begin third-party collections procedures or credit holds at 30 days late, but it is something that surely will be considered by day 60.

Trailing 12 Month Average Days Delinquent: Best calculated at month’s end, the TTADD is essentially DSO minus Best Possible DSO. This allows credit managers to look up historic data on a long-term customer. Often you correlate changes in the number to major events at the company or in the relationship (change of terms, etc.). Some use this to track what effect a credit change had on receivables and cash flow, among other things, related to a specific customer.

Source: NACM-National