

Drive Your eCommerce Business to Success

Table of contents

Here's what's inside:

Introduction	3
Inventory management	4
Having too little inventory on hand	4
Having too much inventory on hand	5
Taxes on excess inventory	5
Managing your inventory	6
Financial issues	6
Cash versus accrual accounting	6
Sales margins	7
Cash flow forecasting	8
Dealing with foreign currencies and international market	9
Currency challenges	9
International taxes	10
Additional considerations	11
Seasonality of goods	11
Protecting your intellectual property	11
Selling for a premium price when you decide to exit	12
Understanding your market	13
Using outstanding customer service to build loyalty	13
Final thoughts	14

Introduction

Although eCommerce was increasing greatly in popularity prior to 2020, in 2020 and 2021 it became a different game entirely. At the same time brick and mortar stores were shutting down, eCommerce sales skyrocketed, in some cases increasing by 300 to 400%.

There were a few causes of this. First, consumers still needed to purchase goods. Being unable to go to physical stores, they turned to online shopping. At the same time, a lot of people were made redundant at their jobs, so they saw an opportunity to make money running an online store.

Running an online store has many benefits:

- Low overhead because you don't have the expense of a brick and mortar location or hiring sales staff;
- Low start-up costs because you can get started from your home; and
- Flexible hours because you are working from home.

While these new entrepreneurs found a great deal of success, many online store owners had corporate or creative jobs before starting their ecommerce business. They weren't necessarily experienced in running businesses, or in dealing with the financial aspect of business management.

This affects them in a few main areas, each of which can drastically impact their success, such as:

- Controlling their inventory
- Managing their cash flow
- Navigating international markets

The good news is you don't need to be an expert in business to be a successful online entrepreneur. There are tips you can follow that will increase your chances of success. Once you're aware of how inventory management and cash flow management affect your business, you can come up with a plan to address those issues.

Additionally, you don't have to make all your business decisions on your own. Having an experienced accountant on your side, who knows and understands the unique ins and outs of online businesses, will help you make the best decisions possible.

1. Inventory management

Inventory management is a common issue among eCommerce businesses. One of the reasons it's so critical is that your inventory management affects your cash flow. If your inventory is well managed, you'll have an easier time with cash flow. But if you struggle with inventory management, chances are you have cash flow issues as well.

Poor inventory management costs retail business owners a significant amount of money every year. Whether those issues are related to not having enough inventory on hand or having too much inventory, they will affect your profitability. When you sell inventory, there's a gap between the time you buy that inventory and the time you receive money from selling it to your customers. During that period, your money is tied up in the inventory. In the meantime, you have to pay your supplier, pay for storage (in some cases) and pay for transportation, among other possible costs.

Not having enough inventory on hand also causes profitability issues for you, because you miss out on sales.

As a business owner, you have to strike a balance between not running out of inventory and not having too much inventory. You need a way to figure out exactly how much you need and when.

a. Having too little inventory on hand

Some business owners are tempted to keep very little stock on hand. But not having enough stock leads to unfulfilled or delayed orders, which results in unhappy customers. Those customers might avoid shopping with you in the future. They may even leave you bad reviews or tell people not to purchase from you.

This is especially concerning if you sell something that's highly niche, making it difficult to get items in a rush. Your customers could buy something from you only to find out there's a long delay before they'll receive the item. Not only does this situation cause problems for you, it could affect your relationship with your suppliers if you're constantly ordering items in a rush.

Supply chain issues can affect how long it takes you to get the products you need to sell. If you're in a period of high demand while facing supply chain problems, some customers could experience massive delays before they receive their orders. If online customers typically expect orders being shipped in 2-3 days, you don't want them waiting up to 3 weeks.

Having ample supply on hand means your customers are likely to receive their orders on time, which goes a long way to fostering positive relationships with your customers. They're also more likely to buy from you in the future, and recommend you to others.

b. Having too much inventory on hand

The opposite is also an issue for online retailers. Having too much inventory means you need space to store it. You'll not only have to pay to store your goods, if there is any excess inventory you can't sell, you'll have to pay for removal costs and possibly even disposal fees. Further, a higher inventory holding means that cash is tied up in inventory, which could cause cash flow issues.

Those costs all add up.

You may wind up in a scenario where you've paid a lot for inventory but aren't recovering those costs right away. You still have to pay all your bills in the meantime, but if your cash is tied up in inventory you won't have enough to cover your bills. Then you're stuck in the position of having excess stock you need to sell quickly just so you can stay operational.

You may also miss out on good opportunities because your cash is tied up in inventory and not available for you to make use of it.

You can mitigate this either by not having too much inventory on hand or by having cash reserves to cover your expenses during the gap between the time you buy inventory and the time you sell it.

c. Taxes on excess inventory

A third significant issue with inventory is that you'll have to pay taxes on your excess inventory. Often when people get into business, they don't realise that at the end of the financial year they have to pay taxes on their unsold inventory.

That's because if you haven't sold something, you can't expense it. So that item goes into your profit and loss statement and it adds back into your profit, making it taxable.

Say you have \$1 million in inventory in your warehouse at the end of the financial year. That now appears on your statement as \$1 million in profit, even if you haven't sold it. You might think you have no profit because there's no cash, but that profit actually sits in your warehouse as inventory.

That's why so many retailers have stock sales at the end of their fiscal year—so they can get money to pay their taxes. Even if they sell an item for well under what they bought it for, at least they don't have to pay tax on the item.

d. Managing your inventory

One method of controlling your inventory is to use a complete, automated inventory system. Such a system tracks how much you order, how much you have on hand, and how well items are selling. It can also track where your products are located in the supply chain and can anticipate future needs based on sales trends. Forecasting your sales cycles will also enable you to anticipate times when you'll need more inventory and times when you can get away with less.

Once you have some data from trading, you may be in a better position to plan the inventory holding.

2. Financial issues

Of course, business owners have to be aware of financial issues related to running their business. Here are some of the main areas we see.

a. Cash versus accrual accounting

Another area that can have a significant impact on your profitability is whether you use cash or accrual accounting. This is the difference between recording cash when you receive the money as opposed to recording it in the month the transaction occurs.

With cash accounting, you record the money when it comes in and goes out. If someone buys from you on November 29 and the money is in your account on December 3, it's recorded as received on December 3.

If you make a purchase from a supplier on January 1 and pay for it on March 10, it's recorded as paid on March 10.

Cash accounting is based on when cash moves into and out of your bank account, and your financial health is based on money you have in the bank.

With accrual accounting, you record income when transactions occur, not when the money is received or paid out. So in the above example, the income is recorded on November 29, regardless of when the money is actually in your account. You also record your company's payments when you incur them, so in the other example, the payment would be recorded as of January 1, even if you don't pay it until March.

This gives you a more accurate picture of how your operations affect your financial performance. You can tell if something you did in November affected your sales, rather than seeing a spike in your profits a few months later and wondering what it's related to.

Accrual accounting gives you a more accurate view of your company's financial health because it includes accounts payable and accounts receivable (what you owe others and what others owe you) in the overall picture. It also smooths out earnings over time, even as profitability increases and decreases. This enables you to make better decisions about your inventory and cash flow, such as tightening your credit policies, offering discounts to encourage early payment, or clearing out excess inventory.

With accrual you need to account for unearned revenue and prepaid expenses, so your financial reporting will be more complex, but you'll have access to more meaningful data that will help you more effectively manage your business. Additionally, with accrual accounting you'll have an easier time preparing financial statements and giving accurate financial information to investors and lenders.

b. Sales margins

Your profit margin is a measure of how profitable your business is. Because eCommerce businesses tend to have low overheads, they may have higher profit margins than retailers with physical locations. Keep in mind, though, that if you have inventory, your expenses likely include transportation and delivery costs, storage costs, and removal and disposal costs.

There are many reasons why you want to know and track your sales margins.

Your sales margins help you:

- Determine whether a product is profitable and worth continuing to sell. If the margin is too low, you can adjust the price, find cheaper materials, reduce the cost of goods sold, or decide not to sell it.
- Allocate resources effectively by providing financial resources to invest in your marketing, research and development, or other areas that enable your business to grow.
- Make informed pricing decisions by enabling you to determine the price point that has the highest impact on your profits.
- Track performance over time so you can identify trends or issues that affect your profitability. This, in turn, enables you to take corrective action if necessary.

Ways to increase your profit margins include increasing your prices, increasing the average value order, and decreasing your expenses.

c. Cash flow forecasting

Successful business owners will use a tool called *cash flow forecasting*, which enables them to estimate how much cash they'll have on hand and how much they'll need to meet their obligations over a set period of time. Having a cash flow forecast enables you to make strategic business and financial decisions.

With a cash flow forecast you'll have better information on when you can spend a bit more money and when you need to tighten up. You'll also be able to anticipate lean times and prepare for them, protecting your business from financial trouble.

When you run an ecommerce business, a cash flow forecast can help you manage your finances during the gap between when you purchase inventory to sell and when you make money off that inventory.

Because your success has a lot to do with timing, creating a forecast can better enable you to plan and schedule your expenses based on your income. It can also give you the motivation you need to tighten up your payment terms, and improve your profit margins.

A cash flow forecast has three main elements:

- Beginning cash balance
- Cash inflows (any cash coming into your business, such as through sales or collections)
- Cash outflows (any expenses, such as utilities and payroll)

In a cash flow forecast, you estimate how much revenue you expect to generate in a time period, based on factors such as historical sales and recent trends. Following that, you look at how much you expect to spend in the same period.

A good idea is to create a best-case, worst-case, and moderate financial forecast, to see where your finances land in each situation. In the case of a recession, it's worthwhile to closely examine your forecast and even revise it weekly, based on changes in the market.

3. Dealing with foreign currencies and international markets

Breaking into an international market is a great feeling.

If you're selling goods overseas, you have a much bigger market to draw from. This means you have a higher potential for income. With that increased potential comes some issues. You'll have to deal with international currencies and exchange fees, both of which affect your margins. You may also have to collect sales taxes and remit those to the government.

a. Currency challenges

i. How currencies affect margins

When you operate in foreign currencies you add a great deal of complexity to your finances. For example, if you receive money in foreign currency, such as US dollars, you have to decide how to record it, whether you'll keep it as foreign currency or transfer it to your currency, and how you'll use that money.

Fluctuating currencies will affect your profit margin. If the New Zealand dollar drops drastically and all your money is in New Zealand dollars, you have to increase your prices to make the same margin. Otherwise, your profitability shrinks.

On the other hand, if you make money off the currency exchange you may have to declare gains on your taxes.

Monitoring currencies minimises your risks, but that takes time and it takes understanding how the currencies work.

ii. How exchange fees affect margins

Foreign transaction fees can have a huge impact on your profitability as well. Although such fees are frequently charged to the buyer, they can be charged to the seller. It's important to be aware of these fees if you work with foreign contractors or foreign suppliers to sell your goods.

Transaction fees to change foreign currency into NZD could cost you up to 20% of your margin if you aren't careful.

b. International taxes

When you sell internationally, you have to be compliant with sales and tax laws in those areas, which can be very different from your local tax laws. Every country, and sometimes even regions within each country, has its own sales and tax rules. You have to be aware of them so you can operate within them. Many online sellers think they don't have to charge taxes if they don't live in the region where their goods are being delivered, but that's not always the case.

In Canada, for example, there's a federal sales tax and a provincial sales tax. If you earn above a certain amount you have to file sales tax with the tax authority—in this case Revenue Canada. Each province also has its own sales tax. Whether you must collect taxes, and how much, depends on the specific goods you provide.

If you get caught not paying your taxes, that's a big problem for you. You'll find yourself paying high fees and penalties. It's much better to be compliant and pay the taxes you owe.

Online sellers who operate internationally are wise to have an accountant guide them through international currencies and taxes to ensure they remain compliant with local laws.

Navigating international markets and dealing with foreign currencies adds a level of complexity to your business you may want some assistance with.

If you have any questions about taking your business international, *please feel free to contact us*. We're happy to answer your questions and give you solutions to make running your business easier.

4. Additional considerations

In addition to the financial and inventory aspects of business, there are a few other issues to be aware of.

a. Seasonality of goods

Not all goods are in demand year round. Some are seasonal, meaning they're only relevant to buyers at certain times of the year. Swimwear tends to have higher sales in the summer than in winter. Ski gear tends to sell more in the winter.

You have to plan for seasonal sales cycles because these affect your cash flow. You'll still have some expenses in the off-season that you have to cover. You'll also want to adjust your inventory so you're not storing a lot of inventory during slow sales times.

b. Protecting your intellectual property (IP)

Because your business is public, you have to take steps to protect your IP, to make sure your product won't be copied by someone else. Most products that you see sold online aren't patented, so they can be easily copied.

While most people can't just go to an online shop and see the turnover, someone who wants to copy you can study your shop and get a sense of how much revenue and visits you have, how busy you are, and whether you're successful. If you're successful, you're more vulnerable to being copied.

For example, sellers can look at what products get positive and negative reviews on Amazon. When they find products that look profitable, they copy the product, change it slightly, then sell it for less.

This creates financial issues for you

There are a variety of ways to protect your IP, which will help you protect your profitability.

- Trademark your brand name, logo, and other identifying business elements to protect against others using them in a way that might confuse customers or decrease your brand's value.
- Copyright your original content to protect your original creative works, including text, images, and videos so others can't use your work without your permission.
- Use nondisclosure agreements (NDAs) with employees, contractors, and partners to protect confidential information, such as business plans, customer data, and product designs.
- Patent your innovations to prevent other people from making, using, or selling your invention unless they get your permission.
- Secure your website and all online assets using strong passwords, two-factor authentication, and updated security.

c. Selling for a premium price when you decide to exit

Often when we start a business, we put all of our thought and energy into getting started, but we don't think about how we want things to look when we exit—or if we ever want to exit.

There are many factors that can make you want to leave your business:

- Someone may make a fantastic offer to buy it
- The business might grow bigger than you expected
- Your priorities shift and you no longer want to run a business
- It's taking up too much of your time
- You've decided to retire or start a different business

Whatever your reasons for leaving, it's so much easier to do when you have a system in place as early as possible. When you decide it's time to leave, having everything in order increases your chances of selling it for a premium price.

This means:

- Having the business set up so it can run easily without you from the first day, or with a minimal transition period

- Knowing the answers to their questions or being able to quickly get answers
- Keeping all relevant reports current and easily accessible

d. Understanding your market

Understanding your market and your competition will help you to be more successful as you build your business.

First, build a client persona so you know who will buy your product—and how many customers you might have. By concentrating on a specific market at first you can get to know your potential customers better, including what their pain points are and how they make their buying decisions.

Second, do a competitive analysis to determine what your competitors are doing and how they're pricing their products. Use this competitive analysis to create a point of difference between you and them. Show your customers what it is that makes you different to other similar products.

Third, create clever marketing based on your point of difference. Engage your audience by showing how you address their pain points, and why your product is better than your competitors.

When you do marketing, be careful to watch your return on investment (ROI). Otherwise, you could bring in a lot of customers but if you're spending a lot of money you might wind up operating at a loss. Look at your cost-per-click and other financial metrics for your marketing, to make sure your efforts are worth the costs.

e. Using outstanding customer service to build loyalty

The value of customer service can't be overstated. Just because you're selling something online doesn't mean customer service gets forgotten. In fact, it can be even more important because you don't have the opportunity to meet customers face-to-face and build that relationship with them.

Customers trust companies that show they care. They also want the confidence of knowing that if they have a problem with a purchase, it can be resolved. After all, you're asking them to give you their credit card number or other payment information. That confidence builds trust and loyalty—and it keeps your customers coming back.

Though it may sound scary to offer instant refunds, the trust they foster makes them worthwhile. Think about the factors that make you more comfortable shopping online and implement them in your e-commerce business.

Final thoughts



Running an ecommerce store is fun and exciting, but it can also be stressful. Being aware of some of the more challenging issues and developing strategies for managing them will help you take your business farther.

At Wise Advice, we're here to help you navigate the complexities of an ecommerce business. *We've helped clients like you* successfully grow their business by implementing easy cloud accounting solutions.

If you'd like to learn more about how we can help you, *reach out to us today.*