

Introduction to Credit Management

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Designed as a quick-reference guide for students, new credit analysts, and anyone interested in the fundamentals of credit management.

1. What Is Credit Management?

Aspect	Description
Definition	The process of granting, monitoring, and recovering credit to ensure that a company's cash flow remains healthy while minimizing the risk of bad debts.
Core Objective	Balance sales growth (by extending credit) with risk control (by limiting defaults).
Key Stakeholders	• Credit department (analysts, managers) • Sales & marketing teams • Finance & accounting • Customers (borrowers) • External lenders & rating agencies

2. Why Credit Management Matters

1. **Cash flow stability** – Timely collections keep operating capital available.
 2. **Profitability** – Proper credit terms can boost sales without eroding margins.
 3. **Risk mitigation** – Reduces probability of defaults, legal costs, and write-offs.
 4. **Customer relationships** – Flexible, fair credit policies improve loyalty.
 5. **Regulatory compliance** – Meets accounting standards (e.g., IFRS 9, ASC 326) on credit risk measurement.
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3. The Credit Management Cycle

1?? Credit Policy ? 2?? Customer Evaluation ? 3?? Credit Approval ?
4?? Contract & Terms ? 5?? Order Fulfilment ? 6?? Invoicing ?
7?? Collection & Monitoring ? 8?? Review & Renewal/Termination

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3.1 Credit Policy

- **Scope:** Types of customers, credit limits, payment terms, documentation, and escalation procedures.
- **Governance:** Approved by senior management; reviewed annually or when market conditions change.

3.2 Customer Evaluation

Tool	Purpose
Credit Scores (e.g., FICO, Experian)	Quick risk indicator.
Financial Statement Analysis	Assess liquidity, profitability, leverage (e.g., current ratio, debt?to?equity).
Trade References	Verify payment history with other suppliers.
Bank Guarantees / Letters of Credit	Provide additional security.
Industry & Economic Outlook	Adjust risk appetite for sector?specific cycles.

3.3 Credit Approval

- **Decision Levels:** Automated rules for low?risk accounts; manual review for medium/high risk.
- **Credit Limit Setting:** Based on cash?flow analysis, collateral, and risk rating.

3.4 Contract & Terms

- **Payment Terms:** Net?30, Net?60, early?payment discounts (e.g., 2/10, net?30).
- **Interest/Finance Charges:** Applied to overdue balances.
- **Security Clauses:** Collateral, personal guarantees, set?off rights.

3.5 Order Fulfilment & Invoicing

- **Order Confirmation:** Verify credit status before release.

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- **Invoice Accuracy:** Prevent disputes; include due date, payment instructions, and reference numbers.

3.6 Collection & Monitoring

- **Aging Schedule:** Categorize receivables (e.g., 0-30, 31-60, 61-90, >90 days).
- **Reminder Process:** Automated emails ? phone calls ? formal letters ? escalation.
- **Dispute Management:** Resolve billing issues promptly to avoid payment delays.

3.7 Review & Renewal

- Periodic re-assessment of credit limits and terms based on payment behavior and updated financial data.
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