Fāilte Ireland
National Tourism Development Authority

GUIDANCE NOTE
CASH BURN & COST REDUCTION

This Guidance Note highlights the importance of critically assessing your businesses cash burn rate and its cost structure. It is accompanied by a series of sectoral Checklists to help you think about where you can reduce costs. The key topics in this note are:

- **Cash Burn Rate**
- **How to Calculate Gross Cash Burn**
- **How to Calculate Net Cash Burn**
- **The Importance of Conserving Cash**

Cash Burn Rate

Cash Burn Rate is the rate of depletion of a business's cash pool in a loss-generating scenario. During this Pandemic, while tourism businesses are closed, it is an important metric to review. Tourism businesses will need to critically assess their cost structure while closed and to understand their burn rate.

A high burn rate could suggest that the business is depleting its cash supply at a faster rate and may indicate a higher likelihood of entering a state of financial distress. Understanding your burn rate will help you to understand when the need will be to seek financial aid/support from banks or other financial institutions. This may be in the form of working capital funding and will provide an estimated timeline of working capital requirement.

The burn rate within the business may not be the same each month. While the business is closed, the costs will predominantly be fixed, however, in advance of the business opening there will be pre-opening costs that will need to be established. During each month of operation, the cost base and cash inflow/outflow will be different as business levels will vary.

These pre-opening costs may include payments to creditors, additional cleaning, health and safety products, payroll, employee training and purchases such as stocks.

Gross Cash Burn Rate

Gross Burn Rate is a businesses operating expenses or the total amount the business is spending each month. It is calculated by totalling all operating expenses including direct costs, variable costs, fixed costs. The burn rate is typically quoted in months. It does not take revenues into account.

Prior Month Cash Balance/ Monthly Operating Expenses = Gross Burn Rate

e.g. March Cash Balance/ April Operating Expenses = Gross Burn Rate (Months)

e.g. €100,000/€10,000 = 10 Months*

(*Based on average operating expense of €10k per month)

We have assumed that the fixed costs of a tourism business during the closed period will be the same each month. However, if there are some months where there is a higher/lower cash outflow then the monthly average (expenses) would be used.

Net Cash Burn Rate

When a business is in operation, you can establish cash burn by determining the Net Burn Rate. This is calculated by subtracting the operating expenses from revenue. It is important to consider that each month you will have fluctuations in revenue. For example, a fall in revenue with no change in costs can lead to a higher burn rate. This is one of the reasons why it is important to understand both your variable and fixed costs.

Prior Month Cash Balance/ Net Operating Income (revenues-costs)

= Net Burn Rate

e.g. €100,000/ €7,000 = 14 Months

e.g. €12,000 (rev) - €5,000 (costs) = €7,000 (net operating income)

The Importance of Conserving Cash

As the severity of the crisis continues to be realised it is critical for all tourism businesses to continually analyse every cost item, however small they may appear, as conserving cash will be key to long-term sustainability.

Please refer to the checklists of cost cutting measures for different tourism businesses which can be explored, some of which may need to be negotiated. This list is a guide and not exhaustive.

It is also important for operators to record all negotiated cost reductions and agreements for a number of reasons;

1. To confirm all renegotiated terms and conditions, e.g. if a supplier has given you a discount for a certain period, confirm in writing when this will end and revert to pre-Covid-19 terms to ensure continued goodwill and understanding of cashflow requirements.

2. Eliminate any discrepancies in the future with suppliers.

3. Analyse and track all cash savings made. It is important to illustrate these if seeking funding as financial institutions/banks may look to see where cost reductions have been made and if there are any further cost reductions available.