CASH & FINANCE

WORKBOOK

How do you make sure your business operates entirely for the purpose of providing you with a profit?

Learn the principles of financial management…Get access to simple measurement tools…Begin working through your own businesses cashflow and breakeven.

Successful business people can tell you exactly how much money they earn, spend and keep…the last one being the most important because that's how you get to have the life you really want. We refer to this as Financial Mastery, and it's the one area of business that tells you how you are going.

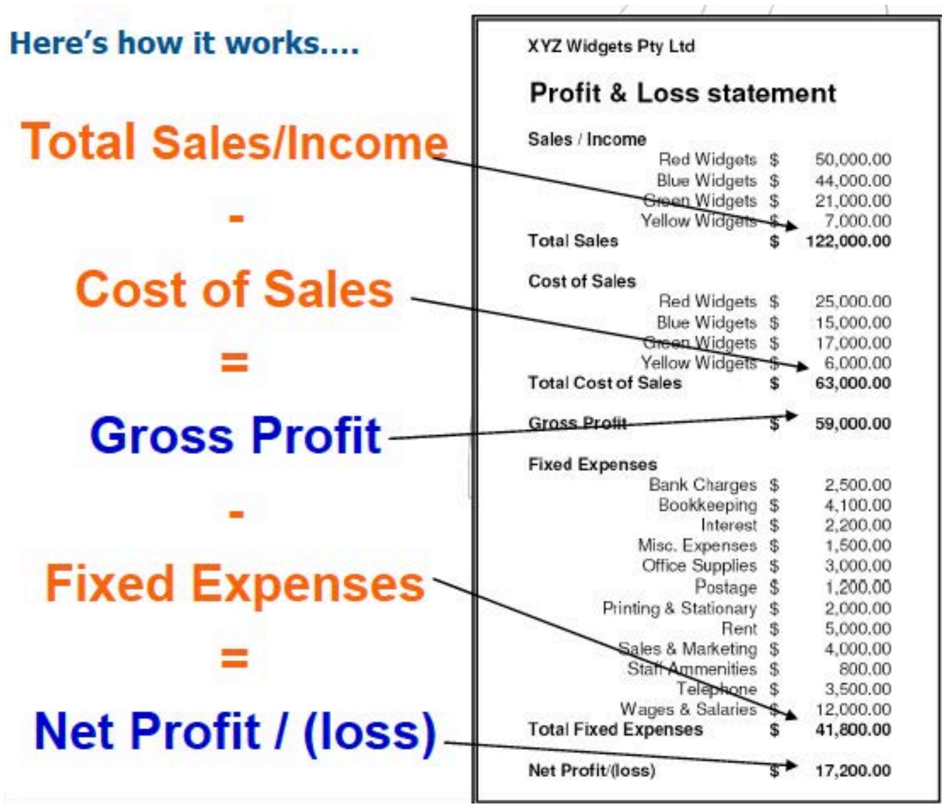
Sadly it's often misunderstood or delegated to the "too hard" basket… "that's the accountants job!" is a typical response.

Well it may be their job, much like you employ people to do the things you choose not to do, but that doesn't mean you don't know how to do those things, or what needs to be done. If you did that it would be called abdication, rather than delegation.

Running your business requires you to know the basics in all areas. Financial Mastery can be complex, but it's not difficult in concept. And that's what we are about to explore…. Have fun…this might appear daunting, but it can be exciting… especially when you see how much money you can make!

The goal of this session is to ensure you recognize the value of understanding your financials and being able to ask the right questions if needed from the people you employ to provide this information. This is a key part of MASTERY in your business.

The Profit & Loss Statement (P&L)



XYZ Widgets Pty Ltd

Profit & Loss statement

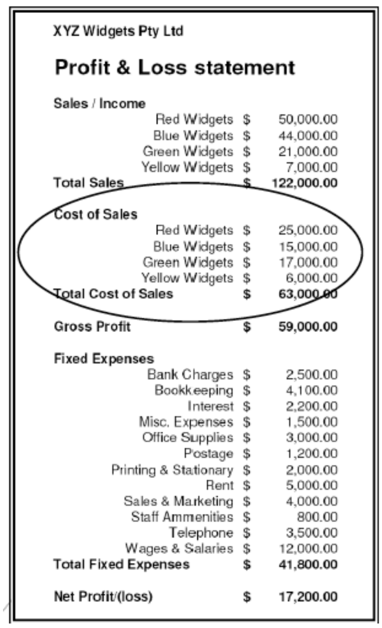
Sales / Income			
	Red Widgets	$	50,000.00
	Blue Widgets	$	44,000.00
	Green Widgets	$	21,000.00
	Yellow Widgets	$	7,000.00
Total Sales		**$**	**122,000.00**
Cost of Sales			
	Red Widgets	$	25,000.00
	Blue Widgets	$	15,000.00
	Green Widgets	$	17,000.00
	Yellow Widgets	$	6,000.00
Total Cost of Sales		**$**	**63,000.00**
Gross Profit		**$**	**59,000.00**
Fixed Expenses			
	Bank Charges	$	2,500.00
	Bookkeeping	$	4,100.00
	Interest	$	2,200.00
	Misc. Expenses	$	1,500.00
	Office Supplies	$	3,000.00
	Postage	$	1,200.00
	Printing & Stationary	$	2,000.00
	Rent	$	5,000.00
	Sales & Marketing	$	4,000.00
	Staff Ammenities	$	800.00
	Telephone	$	3,500.00
	Wages & Salaries	$	12,000.00
Total Fixed Expenses		**$**	**41,800.00**
Net Profit/(loss)		**$**	**17,200.00**

Some Common questions...

What is COS or COGS?

Cost of Sales or Cost of Goods Sold

- This is sometimes referred to as Variable Costs.
- These costs are ONLY incurred when you make a sale…
- This could be the cost of the Product, Delivery, Installation



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COACH TIP:

For example, if you use contractors that ONLY get paid when installing your widgets, then this would be a COS. If your widget installers were paid a fixed wage, regardless of whether or not they did an install, this would be a Fixed Cost.

Is buying stock an expense?

- When you buy stock, this is considered an ASSET to the business and does not get entered into your P&L as an expense.
- Once it is sold it becomes COGS.

So we get consistent figures from month to month we need to record the cost of the Widgets ONLY when we sell them, in the above example we should have $250 profit in each month.

Let's do some numbers...

Firstly lets work out our Gross Margin Percentage...

Sales	______
-	**-**
COGS	______
=	**=**
Gross Profit	______
÷	**÷**
Total Sales	______
X	**X**
100	**100**
=	**=**
Gross Margin	______

Now lets work out what our HIGHEST Gross Margin product is…

For this exercise we will use the same formula, but this time we will do it for each specific product line.

We'll start with Red Widgets…

Calculate the GROSS PROFIT for Red Widgets…

Red Widget Sales = $50,000

-

Red Widget COGS = $25,000

=

Gross profit for the RED Widgets is $25,000

Enter the numbers on to your worksheet opposite on the correct lines.

	RED
Sales	______
-	**-**
COGS	______
=	**=**
Gross Profit	______
÷	**÷**
Total Sales	______
X	**X**
100	**100**
=	**=**
Gross Margin	______

XYZ Widgets Pty Ltd
Profit & Loss statement

Sales / Income			**GP %**
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Total Fixed Expenses		**$41,800.00**	
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ActionCOACH business coaching

Now let's calculate the gross Margin for Blue, Green and Yellow Widgets...

	BLUE	GREEN	YELLOW
Sales	________	________	________
-	-	-	-
COGS	________	________	________
=	=	=	=
Gross Profit	________	________	________
÷	÷	÷	÷
Total Sales	________	________	________
X	X	X	X
100	100	100	100
=	=	=	=
Gross Margin	________	________	________

How can we use this information to increase the net profit?

Now work out how much extra Net Profit you would make if you had the same amount of total sales and ONLY sold Blue Widgets.

Total Sales =	________
x	**X**
Blue Widget Margin @	________%
=	**=**
Gross Profit of	_____
-	**-**
Fixed Expenses of	_______
=	**=**
Net Profit of	_______

COACH TIP:

You can INCREASE your Gross Profit by selling more Higher Margin Goods/Services or re-negotiate with suppliers/Contractors to get lower costs, or simply by Increasing your prices.

You can INCREASE your Net profit by increasing your Sales, your Gross Profit or by reducing Fixed Expenses.

Have a go at thinking a few of your own ideas…

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Profit & Loss statement

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	Green Widgets	$21,000.00	
	Yellow Widgets	$7,000.00	
Total Sales		**$122,000.00**	
Cost of Sales			
	Red Widgets	$25,000.00	**50.00%**
	Blue Widgets	$15,000.00	______
	Green Widgets	$17,000.00	______
	Yellow Widgets	$6,000.00	______
Total Cost of Sales		$63,000.00	
Gross Profit		**$59,000.00**	**48.36%**
Fixed Expenses			
	Bank Charges	$2,500.00	
	Bookkeeping	$4,100.00	
	Interest	$2,200.00	
	Misc. Expenses	$1,500.00	
	Office Supplies	$3,000.00	
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Your Breakeven Analysis

Now let's turn these into a number that is critical for your business…

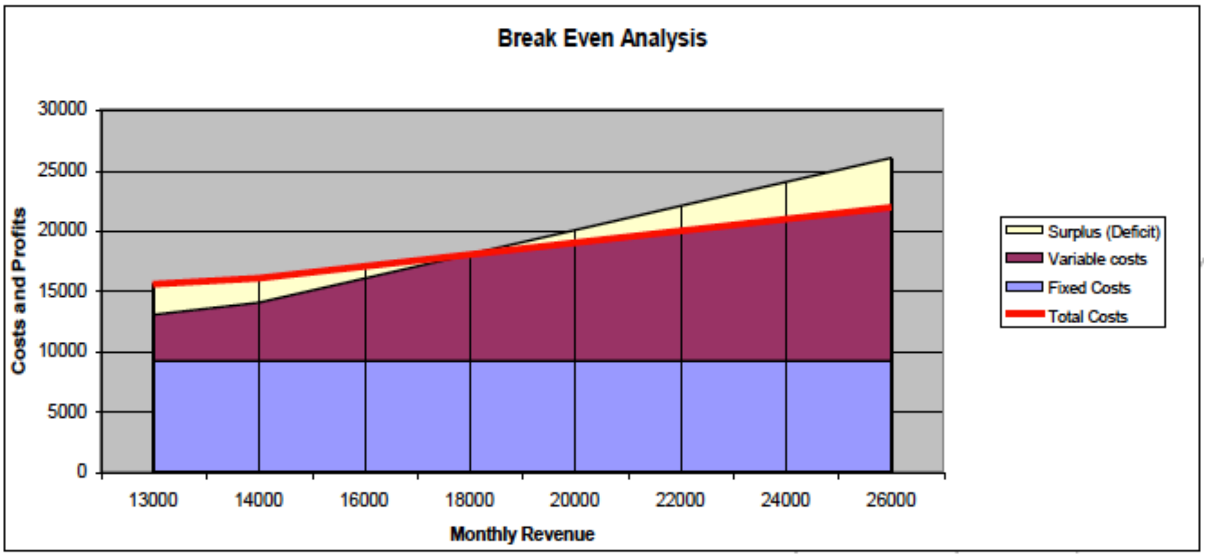
Fixed vs. Variable Expenses

Fixed Expense – Those expenses that you pay whether or not you have sales.

Variable Expenses – Those expenses incurred because you have sales.

Breakeven is the point at which your gross profits cover your fixed costs (overheads).

It is Vital to your business success to know the number of sales you need to Break Even…



Have a go at calculating XYZ Widgets Break-Even... if:

Monthly Revenue	13000	14000	16000	18000	20000	22000	24000	26000
Fixed Costs	9167	9167	9167	9167	9167	9167	9167	9167
Variable costs	6370	6860	7840	8820	9800	10780	11760	12740
Total Costs	15537	16027	17007	17987	18967	19947	20927	21907
Surplus (Deficit)	(2,537)	(2,027)	(1,007)	13	1,033	2,053	3,073	4,093

$$\text{Breakeven} = \frac{FC}{GM\%}$$

Where Break-Even = Revenue needed to break even

FC = Fixed Costs

GM% = Gross Margin %

Gross Margin % = Gross Margin/Revenue

Gross Margin = Revenue – Variable Costs

Now let's practice with Tony's Hot Gog Stand…

- 1,600 people per day pass by the stand; 1 of 4 buy
- Average customer buys 2 sandwiches @$1 each
- Cost of sandwich is $0.25 each
- Customer buys 1x/day
- Fixed Costs = $36K Tony salary; $12K Depreciation
- Business Days = 250
- Purchase Stand $60,000

Use the formula below to calculate the breakeven point…

Fixed EXPENSES	______
/	÷
GROSS MARGIN	______
X	X
100	100
=	=
Break Even Point	____

Answer:

Break-Even = $5,333 per month
FC = $4,000
GM% = 75%

Gross Margin % = Gross Margin/Revenue
Gross Margin = $200,000 – Variable Costs

COACH TIP:

Knowing your breakeven point will ensure you know how many sales you need to at least not have a "gaping hole" each month in your bank account, or in other words, to be in the red. The goal is to be in the black! This point is also critical to the next step, which is your cashflow.

Budgeting

Now let's find out how to make sure you are in control of your cash… The first step is having a Cashflow Forecast

This is where you record:

- SPENDING habits
- CASH on HAND
- LOAN payments
- INCOMING cash
- OUTGOING cash

4 main cash sources

1. Income generated by the business (Sales)
2. Borrowed Cash
3. Sale of Assets, or
4. Capital injection

5 main cash uses

1. General Expenses
2. Purchase of Fixed Assets
3. Purchase of Stock
4. Loan Repayments
5. Owners Drawings

COACH TIP:

A cash flow forecast or budget is a projection of your business's cash in-flows and outflows over a certain period of time. A typical cashflow forecast predicts the anticipated cash receipts and disbursements of a business on a month-to-month basis. However, a cash flow forecast could predict the cash inflows and outflows on a weekly or even daily basis.

NOW let's work through a cashflow budget example…

Cash flow Summary Sheet

- Enter the first Week Ending date
- Enter your Opening Bank Balance
- Enter your Credit Limit if you use a Line of Credit or Over-draft.

Cash In Sheet

- Enter the source of the cash (E.g. Client Name, Outlet etc)
- Enter the amount into the appropriate week ending

Cash Out Sheet

- Enter Creditors, Supplies
- Enter the amount into the appropriate week ending

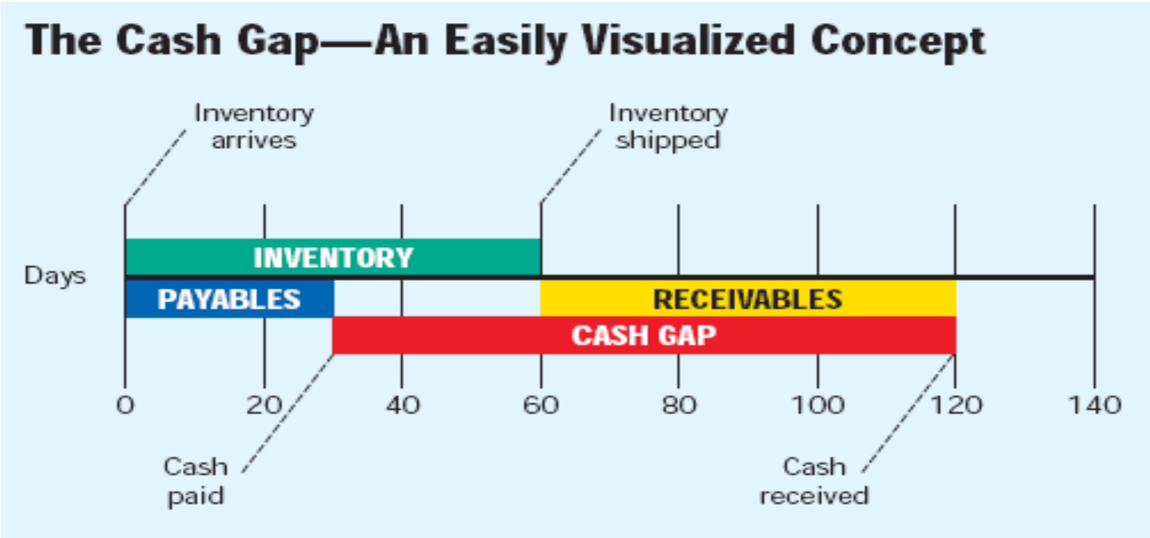
Here's a few idea on how to improve you cashflow…

- Test & Measuring System - for everything
- Put Prices Up
- Add on Sale – Cross sell & Up sell
- Extend Supplier Credit – or any other creditors
- Pre-paid Sales
- Sell Excess Assets
- Use Debt Collection Agency

Another method of changing your cashflow is to manage your CASH-GAP...Let's review that now…

Managing your CASHGAP will make a massive difference to your cashflow...

- The difference between the amount of money you have coming in compared to the amount going out.
- The key is to have it as Positive
- Key components:
    - Payables
    - Receivables
    - Inventory



The Green represents days of inventory, the Blue the days of payables, the Yellow the days of receivables, and the RED—which is determined by the relationship between the first three—is the cash gap.

THERE ARE ONLY THREE WAYS TO REDUCE the Cash Gap:

- Increase the payables period;
- Decrease the collections period; or
- Increase inventory turnover

COACH TIP:

Tradition and the nature of the business often set the typical cash gap in a given industry. Some industries have inherently higher cash gaps than others.

Accounting Records

There are two types of accounting records:

1. Cash basis accounting; and
2. Accrual basis accounting.

Cash basis accounting is used when income and expenses are entered at the time the money actually changes hands, so it's too easy to look at sales and determine you can pay the bills. This type of accounting forces you to manage your money very effectively. It forces discipline. Smaller businesses tend to use the cash basis accounting system. So, if you have no cash, you're out of business! An example of this would be perhaps a $5000.00 sale was made in January, but the payment was not received until March. You actually indicate in the book keeping that the income was in March i.e. received in March.

In **accrual basis accounting**, income and expenses are counted at the time they are transacted. Thus, the $5000.00 –sale would show up in January. Larger businesses generally use this method. The assumption is, yes you have money, but you really don't until you earned it / incurred it.

Ratio Analysis and Financial KPIs

Any number in isolation does not give much of an indication to the quality of the result – there must be a point of reference to enable us to make a judgement.

A key ratio is the 'return on sales' percentage, which is the profit divided by the sales expressed as a percentage.

If the return on sales was 4%, do you know whether this is good or bad.

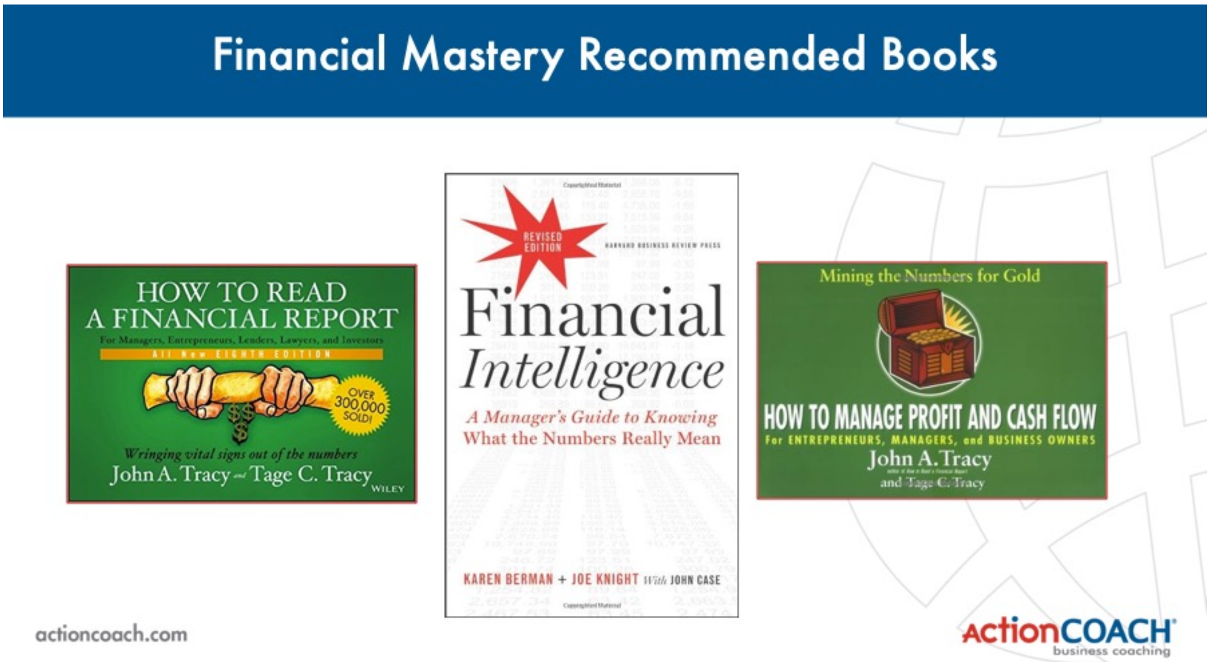
If the industry average is 3% hurrah! Last year they achieved 4.7%, bad news! But the budget was to make 2.5%, good.

Ratios also allow comparative measurements on different sized companies.

The easy ratios to start with are the lines in the P&L as a percentage of the sales figures. They give a guide to the relative importance of the different areas of the business.

Some Example Ratios

Return on Sales	Profit / Sales
Return on Capital Employed	Operating Profit / Capital Employed
Current Ratio	Current Assets / Current Liabilities
Quick Ratio	Current Assets / Current Liabilities Days
Receivables Outstanding	(Accts. Rec. / Annual Sales) * 365
Inventory Turnover	Cost of Goods Sold / Inventory
Interest Cover	Profit Before Interest & Tax / Interest
Dividend Yield	Dividend / Share Price
Price Earnings Ratio	Market Price per Share / Earnings per Share



COACH TIP:

OK there's a lot to get done. By now you should see that it's great to have an idea about being a business owner, but that doesn't automatically make you one. To make that happen you need to do some things differently (change) and implement a few new ideas and activities into your day, week and month.

Enjoy the learning and have fun doing your activities, after all being in business should be **FUN**!

HOMEWORK

1. **Break Even Analysis** — Develop and Evolve YOURS
2. **Reducing Cashflow Gap** — test and measure strategies to reduce the gap
3. **Financial Ratios** – Understand, Implement, and track 3 new ratios / Financial KPIs

Get into ACTION..