Do clients really want to improve the financial performance of their business?

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As a business adviser, and accountant, I am often surprised when I hear business owners say things like:

“Oh, the numbers are nothing to do with me. I leave all that sort of thing to my accountant” or,
“That’s not my job. My job is to keep the sales coming in and everything will be ok”.

I’m sure you have heard similar things said.

I would agree that, unless absolutely necessary, a business owner should not be ***preparing*** financial information for their business. That’s what bookkeepers train for! I’m sure there are much more profitable and rewarding ways the business owners could use the hours they would otherwise spend “doing the books”. It is much more important that they ***understand and use*** the financial information available to them to monitor and improve their business.

When I start working with a new client there are three financial questions I ask to try and gauge how much of an understanding they have of the financial information available to them (if any!).

1. **Is your business as profitable as you want it to be?**
2. **Do you have the cashflow under control?**
3. **Why is there not more money in the bank?**

These questions open up discussions about all areas in their business. These discussions are not just to allow me to get a better understanding of how their business ticks but also to get the business owner to work ***on*** their business for a little while rather than ***in*** it.

One of the best phrases I hear as a business adviser is when one of my clients says, “I don’t know, I’ve never really thought about that before”. This usually means they are starting to think about how their business works and how to make it better rather than just running to stand still.

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1. Is your business as profitable as you want it to be?

More often than not, conversations in this area start with the owner wanting to increase sales and everything will be fine! Sometimes it is worth just getting them to rewind a bit and ask a few questions around how they fit into the business:

- Are you happy with the hours you work?
- Are you earning as much as you would like?
- Will you still be running this business at retirement age?

I find that if you can get them to engage in this kind of questioning you can get a much better idea of how much they want to earn, the hours they want to work, succession planning and perhaps even an exit strategy. This gives them some invaluable information to feed into their financial planning.

I then find it useful to try and get them thinking differently about how to make the business more profitable rather than the standard:

- Increase sales
- Reduce waste
- Reduce costs
- etc

These are important things to address, and can help the business become more profitable, but they may be masking underlying difficulties with the business model they are applying.

Could they increase profit by:

- Reducing sales?
- Increasing cost of sales?
- Increasing overheads?

These questions can appear contradictory for the client but are worth thinking about.

Reduce sales?

Does the client have products, services or customers that it costs money to service? If there is no clear commercial rationale for having these loss making parts of the business, why keep them? I worked with a client who discovered that one of their divisions not only lost money on sales but was responsible for driving a huge slice of overheads as well. As part of a well-managed action plan they were able to exit from this part of their business and increase the overall profitability of their business.

Increase cost of sales?

If additional money were invested in the product offering would they be able to increase prices, perhaps in a different market? One of my clients made lovely little sculptures but it was not until they redesigned the packaging (and increased cost of sales) that they were able to get a listing in a prestigious department store and achieve the premium prices the product merited.

Increase overheads?

I have seen a number of examples where an increase in overheads has lead to a much larger increase in sales. One was a move to more expensive premises by one client. The better address allowed them to open up a new market and charge more for what they were already doing. Another hired a full driver for his factory operation and allowed more of the skilled workers' time to become chargeable to clients.

2. Do you have the cashflow under control?

Most business owners assume that because the money comes in, suppliers get paid and they always stay within their overdraft limit that they have the cashflow under control. This is only part of the story. Can they influence the timing of the payments to enhance the financial position of the business?

Payments

All creditors should be paid in accordance with standard credit terms offered. If the cash is available in the business this may include taking advantage of discounts for early payments. If, however, cashflow will be tight for a period of time I have found that by speaking with key creditors it is usually possible to arrange some flexibility in payment terms. The answer is not always just to try and increase the overdraft.

Receipts

The timing of remittances from customers is less easy to control and can have a major impact on cashflow. Usually negative! Many businesses ask me how they can get late payers to pay on time. Unless absolutely necessary I would prefer not to have "go legal" or charge penalties. I find these approaches can be detrimental to ongoing trading relationships! By the time you are in conflict with a customer over late payment it may be difficult, if not impossible, to get all of the money due to you.

Here are a few things your clients could think about to try and avoid getting into that situation in the first place.

1. Agree in advance what you are going to supply (quantity, quality, timing, etc).
2. Agree payment terms (when, how, etc).
3. For new customers, ask for trade references.
4. Consider doing a credit check if it is a new customer, or an existing customer is placing a large order.
5. Supply what you said you would supply!
6. Invoice as soon as possible.
7. Call to confirm they have received the invoice.
8. A week or so before you expect payment, call to confirm that the invoice has been authorised for payment.
9. Sort out any problems with the invoice as soon as possible (quality, quantity, calculations, etc).
10. Bank the cheque as soon as it is received!

As you can see from the above, taking time to check a few details before, during and after you supply goods or services can help avoid may of the problems relating to late payment by customers.

3. Why is there not more money in the bank?

Just because the profit and loss account is healthy and the cashflow is under control this does not necessarily mean the finances are fully under control.

I worked with a client that was growing profitably and had never exceeded its Euro 800,000 overdraft. They wanted to approach the bank to increase their overdraft to Euro 1M as they anticipated a period of sustained sales growth. As a result of the work we did with them they were able to ***reduce*** their overdraft facility to Euro 500,000 and still fund the sales growth.

The main reason we were able to do this was because their balance sheet was not structured as well as it could be.

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The key areas we examined were:

Stock

Most of the stock items they need could be delivered within seven working days but they were holding approximately eight weeks of stock. We worked with suppliers to ensure the supply chain was robust and were able to reduce the stock held by the business and free the cash for the business.

Debtors

The standard credit terms were thirty days but many of the largest debtors were taking in excess of sixty days to pay. The business had not put formal credit control procedures in place, as they “did not want to upset some of their best customers by chasing them for payment”! A slight change to these procedures resulted in a substantial reduction in the number of debtor days outstanding.

Fixed assets

The business had purchased a number of vehicles and some equipment using the overdraft. In discussions with the bank we were able to get cheaper finance for these items.

The net effect of a few changes in the balance sheet structure was an overall reduction in the amount borrowed from the bank with a corresponding reduction in fees and interest charges.

Many clients don’t see a need to look at the balance sheet because they see profit and cash as being the only things to control. With these clients I call the balance sheet the “Why is the money not in the bank?” sheet and they start to see the benefit of understanding their balance sheet

Conclusion

I hope that this paper may help your clients increase their awareness of some of the business issues that good, regular financial information can help them deal with in their businesses. As an adviser I have found that asking some good questions can often add much more benefit to the business, and the owner, than knowing the answers to the questions they already have.