



5 Ways to Get Real Profits out of Your Balance Sheet

Do you want to have more financial control of your company? Of course you do, or you wouldn't be reading my newsletters. But let's be clear: this is not an attempt to make you into your own controller. We have people who do that for you. Rather, whether your role is CEO, President, owner/operator, senior executive or advisor, if you have some responsibility for guiding a profit-making enterprise, this is for you.



In fact, this is about the opportunity to assess your company's financial health as you set goals for the balance of this year and next. The premise: **The health of your company today is not determined by last year's profit or last year's sales. It's determined by how well you are positioned to make your assets produce a profit for you in the coming year.** And that is best determined by looking at those assets themselves, and the related liabilities, to try to predict the kinds of challenges you'll face in the months ahead. In other words, let's look at your Balance Sheet.



Your company's balance sheet is that financial report frequently overlooked as CEOs scan ahead to see the bottom line number on the income statement. It's the report many CEOs only look at when their banker asks questions about it. But there is a wealth of information in that one-pager – a host of opportunities to improve your business, and your future net worth, by reviewing – and fixing – some of the anomalies that may show up on your balance sheet. Here are five tips that are powerful, yet easy to take advantage of:

1. Does your Quick Ratio – the relationship between current assets and current liabilities – indicate you may have loaned too much money to slow paying customers? If you don't have \$1.50 to \$2.00 in current assets for every \$1.00 of current liabilities, you may be doing more scrambling for cash than you need to. **Speeding up collections is often the simplest and easiest way to raise your cash balance and free up cash for reinvesting in the business.** Ask us for our 5 tips for increasing collections without mutually painful

DID YOU KNOW:
 Ian Fleming, the author of the James Bond novels, was a spy himself during WWII. He served as Director of British Naval Intelligence and commanded an assault unit that became known as Fleming's Private Navy.

- arm-twisting.
2. There should be a substantial difference between accounts receivable and accounts payable, at least in part because your A/R contains a profit margin while your A/P is pure cost. That's an admitted oversimplification since your labor costs are typically in A/R but not A/P, but it's a **very quick way to see if your working capital is out of balance.** I think your A/R should be at least double your A/P. Caveat: if you are paying

your creditors promptly but not collecting from your customers with equal promptness, you've created an imbalance that can starve the business. Consider also stretching your payments to suppliers a bit to narrow the gap. Ask us about "Natural Payment Terms" if you're not sure how to do this.

3. The other major element of working capital for many companies is inventory. **Does the amount invested in your inventory** – even after you write off the slow moving stuff you should have written off years ago – **take up too much of your balance sheet?** How can you tell? Look at a ratio called Inventory Turnover, i.e., how many times a year your inventory completely replaces itself. The computation is Average Annual Cost of Goods Sold divided by Average Inventory. Better yet, do that for each individual high value or low shelf life product you sell. Ask us about a simple inventory control system that will prevent slow moving inventory from getting out of hand (and out of pocket).

4. Then there's your equipment – fixed assets, machinery, vehicles, etc. A quick look at the cost of all that equipment compared to the accumulated depreciation, also on your balance sheet, will show you its Net Book Value ("NBV"). In other words, how much is left to depreciate before those assets are written off the books and in theory used up. If the NBV is low in relation to the original cost of the equipment, you can be pretty sure that either your

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maintenance costs will go up or you'll have to spend money to put new equipment in place – or both. Don't disregard this idea just because you use aggressive write-off methods to save taxes. The concept is still valid regardless of your tax reporting practices. Does it make sense to **buy new equipment that will increase your productivity by 10% if you can borrow the money for 4 or 5%**? Hint: It does if you have the cash to service the debt. If figuring the ROI of all that gives you a headache, ask us to help. We do this all day long.

5. Finally, how about your loans and credit lines? Whether from a bank or a finance company, equipment lender or whoever, if those loans have been on your books for more than 2-3 years and their interest rates have not come down significantly, **you may be overdue to refinance** them to get your cost down to market rates. You should explore that possibility soon, as indications are that rates begin to increase if the economy continues to improve. If your bank won't budge, ask us to introduce you to a more flexible banker. We know some.

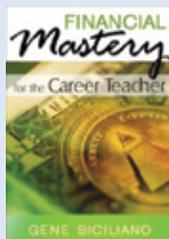
Remember, the ultimate financial pur-

pose of your enterprise is to convert cash to assets and to put those assets to work creating more cash than you invested in the first place. Not profits, cash. Profits are the promise of cash to come, but **cash is the real profit**. And if you don't routinely analyze your company's statements of cash flow – say what? – that balance sheet is the best gauge of cash productivity you've got.



If this is more number stuff than you want to consider, but you can see the possibilities, perhaps you should ask for help. Preferably our help. We wish you a strong growth year with lots of (**cash**) profits in the bank by year end.

CELEBRATING
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