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Create a Profit Plan and Budget for 2013

PDCA Contractor College Webinar

Presented by Linnea Blair

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Do you have a real plan to achieve your revenue and profit goals?

- A detailed and strategic Profit Plan or Budget for the year gives you a framework to achieve success.
- Put your plan in place now, so you can enter the new year already implementing the action steps to make your plan work

If you aim at nothing, you'll hit it every time.

~Author Unknown



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What we will cover today...

- Getting Your Business "On Target" for Success
- Effective Financial Management
- Profit Improvement Planning
- Creating a Budget/Profit Plan
- Key Performance Indicators
- Tracking Job Profitability
- Tracking Your Marketing & Sales



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On the road to becoming an ON TARGET Contractor...





Best Practices: Finance

- Accounting system is fully & accurately functioning
- Controls are in place to ensure accuracy
- A Realistic Workable Profit Plan (aka Budget) is in place
- Financial Monitoring is being used effectively as a business tool
- Key Metrics are being used to keep your finger on the financial pulse of your business
- Owner reviews Financial Data and Metrics at least monthly
- An adequate credit line is in place
- Company is profitable, solvent and able to finance its growth and reward stakeholders

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Profit Planning

How to Increase Your Bottom Line

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Your Business is an Investment to Make Money

To do this, you must simultaneously increase three things:

- Net Profit
- Cash flow
- Return on Investment (ROI)

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Definition: Profit Margins

- Gross Profit = What's left over after you deduct direct job costs from the revenue your business generates

Gross Profit = Total Income – Direct Expenses to Produce jobs

- Indicator of the productivity of your field crews
- Indicator of the accuracy of your estimator (and pricing)

- Net Profit = What's left over after you deduct ALL expenses from the revenue your business generates

Net Profit = Total Income – Total Expenses

- THE bottom line in your business
- Indicator of the overall management of the business

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How To Calculate Profit Margins

- Gross Profit Margin (GP%) is profit derived from work produced divided by Gross Revenue
$$\text{Gross Profit Margin} = (\text{Gross Profit} / \text{Revenue})\%$$
- Net Profit Margin (NP%) is after-tax net profit divided by Gross Revenue
$$\text{Net Profit Margin} = (\text{Net Profit} / \text{Revenue})\%$$



Key Profit Drivers

- Work with these Key Profit Drivers to improve profitability
- Focus on the areas where most potential increase in profit is possible
- *Price*
- *Volume of sales*
- *Variable costs*
- *Fixed costs*



Pricing Strategies

- You can increase profit by **increasing** price
as long as you don't lose so much business that it reduces your net profit
- You can increase profit by **decreasing** price
as long as you increase volume enough to achieve your net profit

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How Much Additional Volume Do I Need If I Cut My Price?

%	GROSS PROFIT MARGIN				
	35	40	45	50	55
4	13	11	10	9	8
6	21	18	15	14	12
8	30	25	22	19	17
10	40	33	29	25	22
12	52	43	36	32	28

Price Decrease →

Volume Increase To Give Same GP

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Discount Price by 10%



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What Volume Can I Afford To Lose If I Increase My Price?

	%	GROSS PROFIT MARGIN				
		35	40	45	50	55
Price Increase	4	10	9	8	7	7
	6	15	13	12	11	10
	8	19	17	15	14	13
	10	22	20	18	17	15
	12	26	23	21	19	18

Volume Decrease To Give Same GP

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Increase Price by 8%



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Volume Of Transactions

- You can increase profit by **increasing** volume of sales
 - provided that price remains constant so that the increase in volume translates in higher gross profit
- OR
- You can increase profit by **decreasing** volume of sales
 - provided that the resulting cost savings outweigh the reduction in gross profit from the decrease in volume



Cost Strategies

- Increase Gross Profit by reducing Direct Costs
 - Labor
 - Materials
- Keep Variable costs equal or below the rate of increase in sales revenue
- Achieve greater productivity from Overhead (Fixed) Costs

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Cost Definitions

- **Direct Costs:** Costs directly related to the production of revenue.
- **Overhead (General & Administrative) Costs:** These costs are generally fixed but some may be variable as well
- **Variable Costs:** Costs that can vary directly with sales revenue. Generally related to production but not a direct job cost
- **Fixed Costs:** Costs that are incurred whether or not any sales are made.

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Increase Gross Profit Margin

To improve the Gross profit margin you need to work on these drivers:

- Pricing & Estimating
- Material Costs
- Labor Costs
- Production / service delivery processes
- Team Skills and Development
- Customer Relationships (Profitable Target Markets)

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Lower your direct costs and Increase your gross profit

- Decrease Cost of Labor
 - Decrease average wage on crews
 - Increase efficiency – bring jobs in on time
- Decrease Cost of Materials
 - Increase Materials Markup
 - Better Estimate of Materials Cost
 - Negotiate better prices with vendors
 - Purchase in bulk

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Working with Direct Costs



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Improving The Net Profit Margin

To improve the Net profit margin you also need to manage the following:

- Administrative operating processes
- Variable Costs
- Overhead Costs
- Administrative Team Skills and Development
- Marketing Activities and Costs
- Customer Relationships

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Profit Planning Summary

- So far we have focused on profit improvement strategies...how to make more money
- We've covered the three key profit drivers: price, volume and cost
- You've seen the impact of discounting prices as compared with increasing your prices
- We have looked at how you can analyze where the potential for Profit Improvement lies within your business
- Remember the phrase 'What you can measure you can manage'



Creating a Budget to achieve your Profit Plan



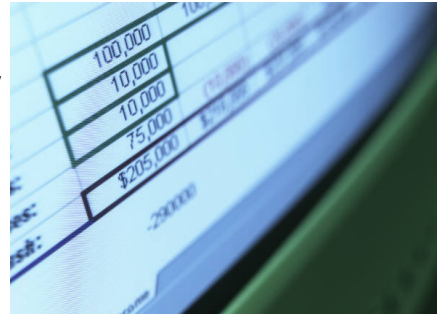
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Get to know your numbers

- Shape up your Chart of Accounts and Bookkeeping
- Plan for success – the budgeting process (informed by your business plan)
- Stay informed with timely reporting
- Know the score with ongoing monitoring of actual to budget performance



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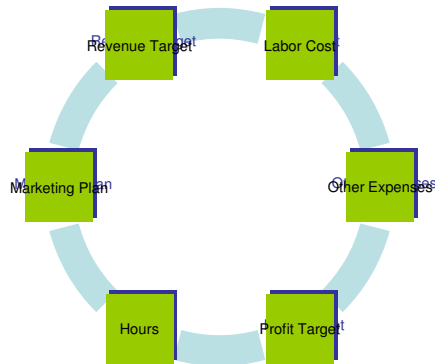
The Budgeting/Profit Plan Process

- Review your Business Plan
- Use your 2012 Monthly Profit & Loss Report as a guide
- Create a Budget/Profit Plan
- Project labor cost and hours
- Evaluate other changes in expenses
- Ensure budgeted hours will meet revenue targets
- Re-evaluate all components



Use Design Spiral Thinking

- What is revenue target?
- What is projected cost of direct labor?
- What other expenses need adjustment?
- Does budget achieve profit target?
- Do hours support revenue target?
- Should revenue target be adjusted?
- Does marketing plan support revenue target?



Let's look at an example...





Monitor your Progress

- Incorporate Budget into QuickBooks
- Monitor Monthly & YTD Progress
- Make management decisions to achieve plan
- Identify Action Steps for upcoming month



Best Practice Guides

Some Metrics to Watch



BEST PRACTICE GUIDE : Gross Profit %

$$\text{Gross Profit Margin} = \frac{\text{Gross Profit}}{\text{Revenue}} \times 100\%$$

- Higher is better
 - 50% is goal
 - 45% is industry average*
- * Residential and Commercial Contractors under \$10MM, depends on mix of work, and use of subcontractors

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BEST PRACTICE GUIDE : Net Operating Profit %**

$$\text{Net Operating Profit Margin} = \frac{\text{Net Operating Profit}}{\text{Revenue}} \times 100\%$$

- Higher is better
- 15% is goal (25% BEFORE Owner's Compensation)
- 5% is industry average*

* Residential and Commercial Contractors under \$10MM

** There is a distinction between Net Profit and Net Operating Profit, which is Profit before taxes, and "other" income & expenses not related to operations of the business

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BEST PRACTICE GUIDE : Breakeven Sales

$$\text{Breakeven Sales} = \text{Overhead Expenses}^* / \text{Gross Profit Margin}$$

- Calculate by week, month, or year to manage your business effectively and keep a positive bottom line

*Include Variable Costs, Overhead Costs and “Other Costs” if critical to business survival

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Need help to grow a sustainable business?

- On Target for Contractors Program
- Business Plans
- Marketing Plans
- Business Webinars
- Business Health Check-up
- Social Media Consulting
- **NEW: On Target 10 Week Intensive – Next session begins January 29, 2013!**
 - Find out more at AdvisorsOnTarget.com

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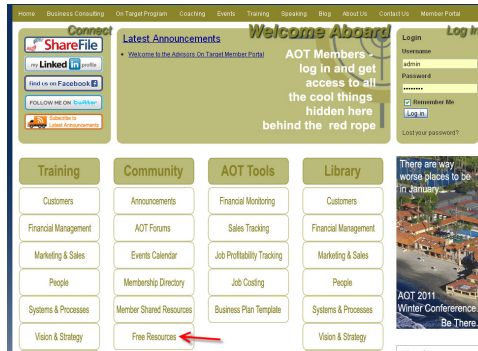
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Sign up as a free member –
then log in to access



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Contact me to get your business On Target
for success in 2012 and beyond!

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