

# Create A Profit Plan for a Successful 2011

presented by  
Advisors On Target

## PDCA Contractor College November 16, 2010

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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...

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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 Improvement Strategies:

or How to Make More Money

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Key Profit Drivers

Work with these Key Profit Drivers to improve profitability and to focus on the areas where most potential increase in profit is possible

- Price
- Volume of sales
- Variable costs
- Fixed costs

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## 1: Working On Price

- You can increase profit by **increasing** price  
provided that any resulting reduction in volume does not offset the effect of the price increase on the profit margin
- OR
- You can increase profit by **decreasing** price  
provided that the increase in volume is sufficient to offset the reduction in profit margin caused by the reduction in price

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

%	GROSS MARGIN				
	20	25	30	35	40
4	25	19	15	13	11
6	43	32	25	21	18
8	67	47	36	30	357
10	100	67	50	40	33
12	150	92	67	52	43

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

%	GROSS MARGIN				
	20	25	30	35	40
4	17	14	12	10	9
6	23	19	17	15	13
8	29	24	21	19	17
10	33	29	25	22	20
12	38	32	29	26	23

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## 2: Working On 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

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## 3: Working On Costs

Working Definitions

- Variable Costs:** These costs can vary directly with sales revenue, in other words when sales rise or fall, they rise and fall.
- Fixed Costs:** These are those costs that are incurred irrespective of whether or not any sales are made. They are usually associated with the physical capacity of the business to provide its service to customers.

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## Working On Fixed Costs

- You can increase profit by **reducing** fixed expenses
  - provided that sales revenue does not decline or if it does, the reduction in revenue is less than the saving in fixed expenses.

OR

- You can increase profit by **increasing** fixed expenses
  - provided that there is a resulting increase in gross profit from greater market share or higher gross margin.

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### Working On Variable Costs

- You can increase profit by **decreasing** variable or activity related expenses
  - provided that there is no change in product or service **quality** that could have a consequential effect on sales volume
- OR
- You can increase profit by **increasing** variable or activity related expenses
  - provided that the improvement in product or service quality allows you to win greater market share or premium price

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### Profit Improvement Strategies Summarized

- Increase sales revenue by increasing price and/or volume
- Keep variable costs at least equal to or below the rate of increase in sales revenue
- Achieve greater productivity from the resources which are financed by overheads

The key is to understand the likely outcomes of each strategy. Proper planning allows you to work through each potential scenario and reduce business and financial risk.

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### Drilling Down Into Profit Improvement Planning: Understand The Components Of Sales Revenue

**TOTAL REVENUE = Total Customers x Number of Transactions x Average Sale Value**

**TOTAL CUSTOMERS** = Number of customers at start - customers lost + new customers

**NUMBER OF TRANSACTIONS** = The number of times each customer deals with you

**AVERAGE SALE VALUE** = The average value of each sale

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## How To Increase Total Sales Revenue

- Get more customers
- Improve customer retention rate
- Improve return visit rate
- Improve average sale value

AND

- Have customers recommend you to their friends and associates

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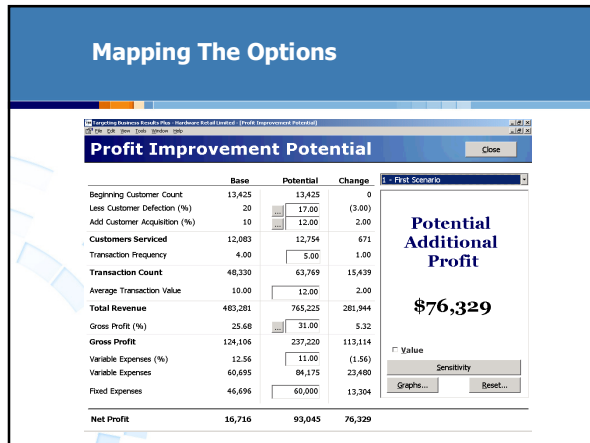
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## Mapping The Options




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## Summary

- This module has 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
- It's all about the phrase 'What you can measure you can manage'

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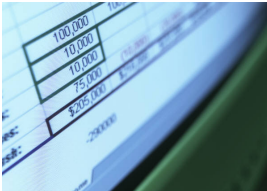
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# Creating a Budget to achieve your Profit Plan



# 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

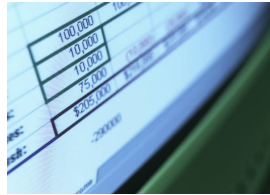


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- Shape up your Chart of Accounts and Bookkeeping
- Plan for success – the budgeting process (informed by your business plan)
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- Know the score with ongoing monitoring of actual to budget performance





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# The Budgeting/Profit Plan Process

- Review your Business Plan
- Use your 2010 Monthly Profit & Loss Report as a guide
- Create a Profit Plan
- Implement Hours/Compensation tool to project labor cost and hours
- Evaluate other changes in Expenses
- Ensure budgeted hours will meet revenue targets
- Re-evaluate all components

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### 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?

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### Let's look at an example...

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### Benchmarking Stats

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### Benchmarking Averages

- Direct Costs
  - Materials
  - Labor (without burden)
  - Subcontractor
- Gross Profit Margin
- Variable Costs
- Overhead Costs
- Net Operating Profit

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### Monitor your Progress

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

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### Key Metrics

Other Important Financial Data to Watch

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### Liquidity Ratios

Current Ratio =  $\frac{\text{Current Assets}}{\text{Current Liabilities}}$

Should be a *minimum* of 1.5 or higher (3.0 or greater is better)

Quick Ratio =  $\frac{\text{Cash + Equivalents}}{\text{Current Liabilities}}$

Should be at least 1.0

Higher is better for both

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### Return on Assets (ROA)

Return on Assets =  $\frac{\text{Net Income}}{\text{Average Total Assets}}$

Higher is better

Should be at least 10%

25% or higher is a goal

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### Debt Ratios

Debt Ratio =  $\frac{\text{Total Liabilities}}{\text{Total Assets}}$

Should be less than 1.0

Debt to Equity Ratio =  $\frac{\text{Long Term Debt}}{\text{Stockholder's Equity}}$

Should be less than 1.5 or 150%

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Days Sales Outstanding

Accts Receivable x 365

Days Sales Outstanding = 

Annual Revenue

(previous 12 months rolling revenue)

Should be 30 days or less

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Breakeven Sales

Overhead Expenses

Breakeven Sales = 

Gross Profit Margin

Calculate by week, month, or year

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Cash in Bank – Ideal

Overhead Expenses (next month)

Cash in Bank = 

Gross Profit Margin

Plus: Fixed expenses for months 2 & 3

Or – just think 3 months fixed expenses for a quicker calculation

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## Benchmarking Averages

- Current Ratio
- Debt Ratio
- Days Sales Outstanding


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## Connect with us to see how you can get your business On Target for success!

4 Free Things You Can Do Today

- Go to [AdvisorsOnTarget.com](http://AdvisorsOnTarget.com) and Sign Up for our Email Updates
- Click On Member Portal and Sign up as a Free Member to have access to our Free Tools
- Go to Facebook and “Like” our Business Page at [facebook.com/AdvisorsOnTarget](https://facebook.com/AdvisorsOnTarget)
- Follow us on Twitter at [AdvisorOnTarget](https://twitter.com/AdvisorOnTarget)

If you need more help with budget/profit plan for your business just give me a call at 619.291.3700


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## Contact Info

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