

Illawarra Small Business Assistance

HELPFUL HINT - HOW TO AVOID THE “CASHFLOW VERSUS PROFIT” TRAP

Despite good intentions and due to preoccupation with time pressures and daily problems many small businesses fail to give adequate attention to their financial future until severe difficulties develop.

However, many common business problems can be overcome or avoided with adoption of basic planning procedures in the areas of pricing, operations and marketing.

Early identification of problem areas is crucial. With well planned appropriate corrective action including financial reorganization and the availability of budgets and management reports from which to monitor and regulate performance, survival can most often be achieved with reasonable prospects of sustained recovery over time.

In an earlier “Helpful Hint” I highlighted how critically important it is not to mistake profit with cash flow. It’s rather unfortunate that many writers of financial articles encourage the view that small businesses should direct most attention to the generation of sales and cash-flow to fund working capital needs. This approach is mostly predicated on the belief that individual products and services are priced appropriately. However, in reality this is quite often not the case.

As outlined by Tracey Collins in the “Pricing for Profit” workshop held at Austinmer in 2007, emphasis on selling those products and services that achieve a profit margin lower than the overall target gross profit margin required for the business as a whole may be counter-productive and lead to reduced profitability. The consequences of this may be that although overheads might still be covered there could be little or no margin available to reward proprietors.

To ensure your business doesn’t fall into the “cash-flow versus profit” trap it is vital to understand the concept of “breakeven” and to know the gross profit margin for each major product or service line, as well as the overall gross profit margin for the business.

With this information it is possible to run “what if” scenarios to assess whether or not individual products/services will help the business achieve its profit targets.

We will be pleased to provide you with a copy of the presentation as well as the spreadsheet templates that will assist you to work out the breakeven for your business and conduct a profitability analysis.

CONTACT:

For further details and assistance, please contact:

Dick Bradley

Illawarra Small Business Assistance

Tel: 02-4227 4500 Mobile 0431 101 228

Email: smallbusiness@rdaillawarra.com.au

Website: www.illawarrasmallbusiness.com.au