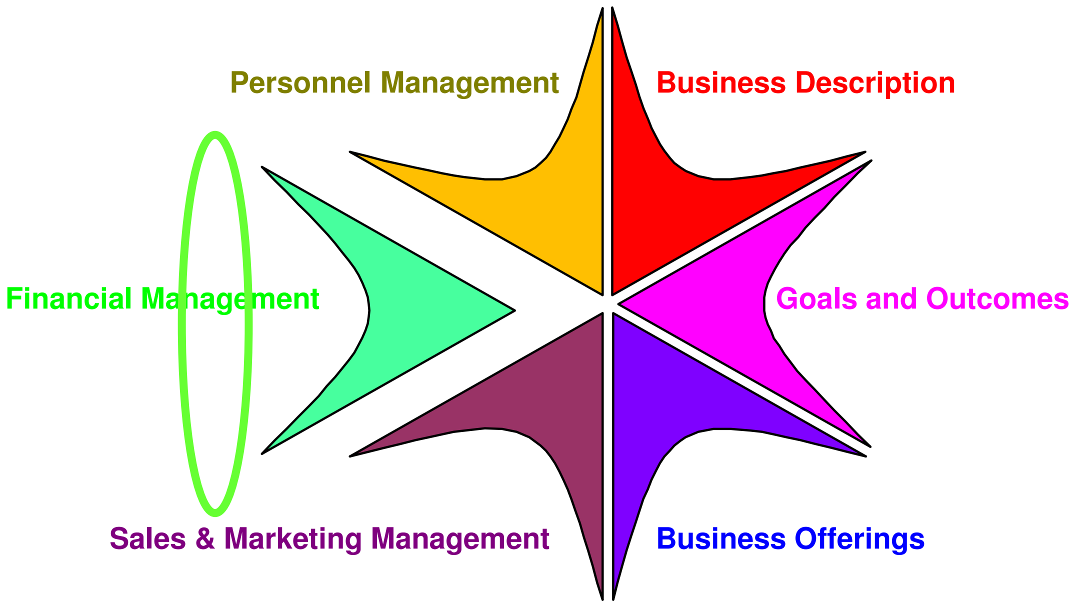
Financial Management



BizBite CONSULTING GROUP

Learn Today... Profit Today

Table of Contents

Financial Data—the heart of the business

"Wherever you see a successful business, someone once made a courageous decision."--Peter Drucker

Introduction

Before you turn a wheel, sell a *widget*, or accept a contract, it is essential that you decide how you will keep track of the transactions that are made. Good accounting for your business is important because of legal and tax requirements.

A good accounting system provides you with the tools you need on a daily basis to take the pulse of your business and make the positive business decisions that will keep it healthy and on track.

It should be tailored to your business needs and be simple enough so that it can be maintained on a daily basis. This is how you control your business, know where it has been and know where it is going.

Control is essential!

If you don't control your business, your business will control you!

Break-even Point (BEP) Analysis

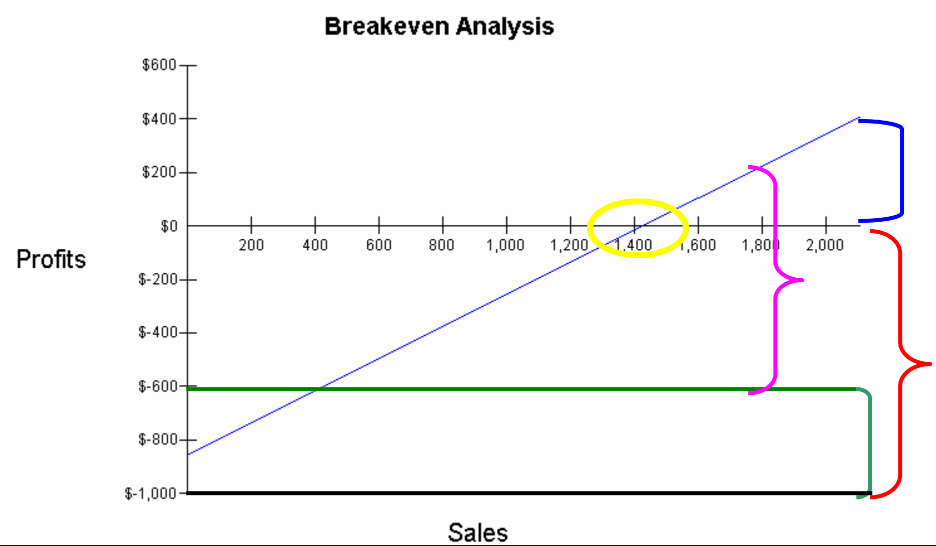
Introduction to break-even point analysis

The ***break-even point analysis*** is one of the most important tools in assessing the viability of pursuing new ***market segments*** as well as the relative return on investment of various existing market segments.

A ***break-even point (BEP)*** is the point where the business' total costs will just equal its total revenue.

> If you know the break-even point, you have a definite target to shoot for and can put a step-by-step strategic plan together to achieve the goal.

For example



Legend	
Red bracket indicates the loss area **Pink** bracket indicates <u>total variable costs</u> **Green** bracket and line indicates <u>total fixed costs</u>	**Orange** bracket indicates profit area **Yellow** oval indicates the break-even point

Job Costing Analysis Preparation

Introduction

It is important for every business to accurately determine its fixed costs and variable costs. After that, the business must ensure that these costs are at least offset by the revenue the business generates from the sale of its offerings.

In **Job Costing Analysis Preparation**, we will first demonstrate how a business analyzes and determines it's fixed and variable costs.

Later in ***Break-even Point Analysis***, we will discuss how the business uses information on fixed and variable costs to:

- Test the profitability of the business.
- Project the viability and profitability of venturing into new markets.
- Project the viability and profitability of new offerings.
- Price offerings on a daily basis at levels that will ensure projected profits.

In **Job Costing Analysis Preparation**, we will explain how a company analyzes its fixed and variable costs and then ensures that the business recovers those costs and an adequate profit margin in the pricing of its offerings in every segment of business activity.

For illustration purposes and simplicity, we will use a fee for service business. It is an architectural services company managed by the owner and five staff.

As you move through this example, ask yourself how the ideas and methods presented here would apply to your business.

The ideas discussed here may be used in any type of business. Every business situation will be different so be prepared to customize this process to meet your company's needs.

The job costing process

The job costing process has six steps:

- **Research fixed costs**
- **Determine revenue necessary to offset fixed costs**
- **Calculating employee charge rate to recover costs**
- **Segmenting services**
- **Analyzing**
- **Arriving at a price**

Step #1—research fixed costs

Begin by thoroughly researching the fixed costs of the business for at least the past two years.

The purpose is to arrive at a base figure that accurately represents the total annual fixed costs.

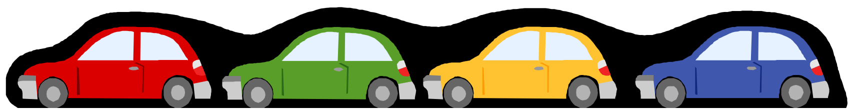
With some expenses, you may want to take an average of the cost over the two-year period. It is really for you to decide if periodic fluctuations in a cost warrant averaging the cost.

You should adjust the base fixed cost figure to reflect any estimated growth or decline in fixed costs to arrive at your estimated annual fixed costs.

Fixed cost items would include:

Rent	**Mortgages**	**Long term loans**
Heat	**Light**	**Telephone**
Building maintenance expenses		**Administrative**

If this were an example of the Aged Accounts Receivable Report for your business, the following observations might be made concerning the accounts:



Acme Supply—This delinquent account is getting further in debt to your company every month.

It is clear that only partial payment is being received for each month's purchases.

The reason for this should be determined immediately.

If the customer has kept the account more current in the past and is a valued account, you may wish to negotiate a regular payment schedule to retire the past months owing.

You may even wish to continue selling to the customer as long as they adhere to the payment schedule.

If the circumstances don't warrant a negotiated repayment schedule, then the customer's account should be suspended until the account is brought into line with the credit terms policy of your company.

If no effort has been made to repay the amounts owing, it may be necessary to either sue the customer for the money or send the account to a collection agency.

Glossary

Balance Sheet

The balance sheet records what the cash position or liquidity is of the company. It is also records what the owner's equity is in the business at a particular point in time. The balance sheet shows the result of the daily operating decisions of the company.

The Balance Sheet really summarizes:

- The affect on the business to date of the operating decisions of the past.
- It shows how the assets, liabilities, and net worth of the company are distributed.
- It shows how the assets, liabilities, and net worth of the company have been affected by operations up to that point in time.

All balance sheets record the same information and have the same categories. The only difference is the amount of detail that is shown and that will vary with the complexity of the business.

Booking orders

Break-Even Point (BEP) Analysis

The Break-even Analysis is based on the Income Statement and the Cash Flow Statement. It shows the amount of revenue that the business needs to exactly balance the fixed and variable expenses.

No business manager can ignore these facts no matter how large or small the business is. This information is critical for making important decisions in areas such as:

- Setting price levels.
- Whether to purchase or lease new equipment.
- Projecting profitability at different volumes of business.
- Whether it is feasible to hire another employee.

The break-even point analysis affects every area of the business. For more detailed information on the use of Break-even Analysis please refer to the section where it is dealt with in detail.