BUSINESS EVALUATION GUIDE

ISBN 978-0-6487513-2-8

TABLE OF CONTENTS

INTRODUCTION

It is crucial to regularly review how your business is progressing, identify how you can make the most of your market position, decide where to take your business next and what you may need to do to get there.

This guide is the first in a three-part series providing guidance on how to:

- assess your business performance
- identify your strengths and areas for improvement
- implement the improvements you have identified.

Evaluating business performance will give you much of the information you need to determine:

- how well the business is performing
- whether the business is making the most of its opportunities
- if the business plan remains relevant
- if the business is moving in the direction you want it to go
- if the business is becoming unresponsive to market demands.

Continuous evaluation of your business' performance informs you of what works and what does not work. Ongoing assessment also helps you determine if your business is ready to grow or change direction, including entering new markets, and what you have to do to achieve that.

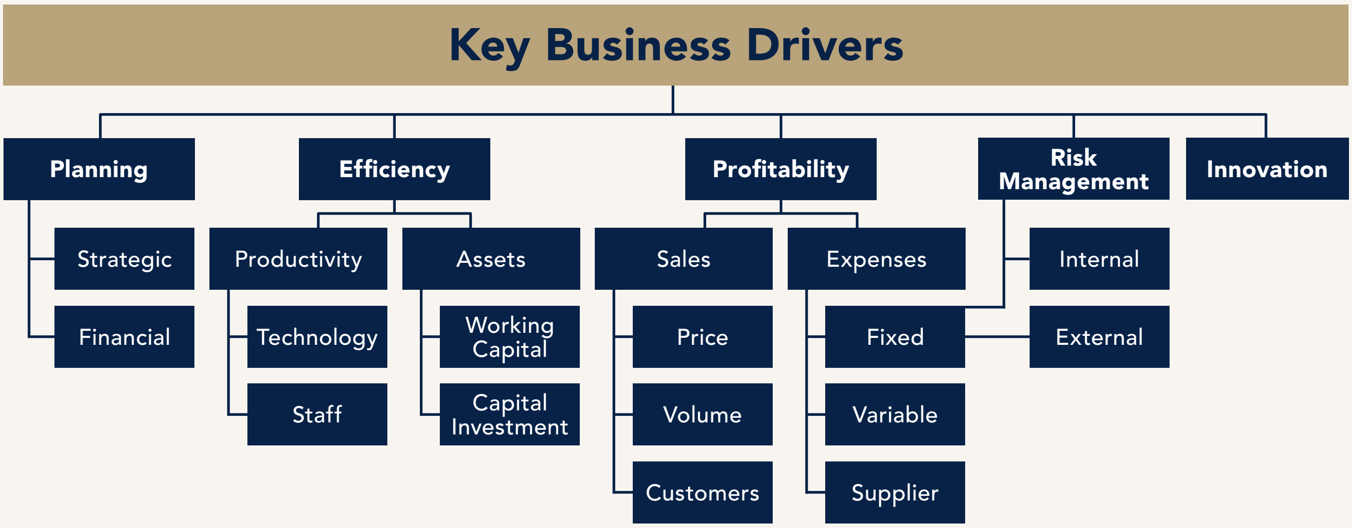
Before undertaking an evaluation, it is important to have a detailed understanding of how the business operates and what the key drivers for the business are (see below chart of examples of key business drivers). This will help develop a more structured and meaningful evaluation. However, there is no standard template to evaluate a business – every business is unique and the key drivers for each business will vary.

You may not be able to undertake the business evaluation on your own. Good businesses rely on expert advice, so involve your professional advisers and key personnel (e.g. your management team and senior staff) to make your review more effective.

This guide is intended to help business owners, managers, accountants and other business advisors implement a business performance evaluation method for their business (or the client's business).

COMMON EXAMPLES OF KEY BUSINESS DRIVERS

Business drivers are the inputs and activities that drive the operational and financial result of a business. Some examples include the size of the sales force, the price of products sold and the volume of products sold.



EVALUATING PERFORMANCE

As part of evaluating your business, you should look at:

- **Your market performance and direction** – how strong are your sales results, what are the characteristics of your current market and how might that evolve?
- **Your products and services** – consider how long your existing products or services will meet your customer needs and any plans for renewal?
- **Operational matters** – are your premises, processes and technologies meeting your needs and the needs of customers? Consider if there any internal issues that are holding your business back?
- **Financial matters** – how your business is financed, levels of retained profit, the sales income generated and sales flow.
- **Your organisation and your people** – consider the skills of your staff, their training and development needs as well as your organisational structure.
- **Your strategic plan** – consider whether the current business operations are on track to achieve the plan?

SETTING OR RESETTING YOUR BUSINESS STRATEGY

Having a clear business strategy will allow you to effectively assess business performance.
In setting or reassessing your strategy, ask:

- What do I want to achieve in my business?
- What are my key measures of success?
- Am I satisfied with the current performance of my business – is it meeting my expected return on investment and am I happy running the business?
- What do I want my business to be doing in three to five years? What are my measures for success at that time?
- How do I intend to get my business from where it is today to where I want it to be?
- Do I have the right products or services to achieve my objectives?
- Which markets do I want my business to compete in? What does my business have to do to effectively compete in those markets?
- What do my current and future competitors do better than my business? What does my business do better than them?
- What external factors may affect my business? Consider the political, economic, social, technological and environmental factors.
- What skills, assets, finance, networks and technology do I need to compete?
- Do I have the right team, culture and technology to help me take the business where I want it to go?
- If I don't have access to the resources required, how do I get access or adapt my business?
- Can I break down my measures of success into key performance indicators?
- Contact your banker to learn about loan refinancing options (sometimes you may be able to obtain a lower interest rate or lower the monthly payment).

REVIEWING PLANS, BUDGETS AND FORECASTS

All business evaluations should include a review not only of the financial aspects of the budgets and forecasts, but also how closely they support the strategic plan.

The evaluation should consider:

- the frequency of the preparation of a strategic plan, budget and forecasts (while budgets and forecasts should be done regularly, regular strategic plans may be counterproductive)
- the assumptions that have been used in developing the plan, budgets and forecasts, including the reliability of the assumptions
- the authorisation process of the budgets and forecasts, such as whether the forecasts are approved by the owner or board
- the reporting mechanisms used to track the implementation of the strategic plan, and how budgets versus actuals are reported and monitored.

CASE STUDY: BUNDALONG RETAIL PLANT NURSERY (“BUNDALONG”)

To illustrate how a business evaluation model is developed, a case study is included in this guide. The case study provides an overview of the key drivers of a retail plant nursery.

The financial statements of Bundalong are included in the **Appendix A**.

BACKGROUND

Bundalong retail plant nursery is situated in a rural town which has a population of approximately 38,000 residents. The nursery has been operating for 15 years and in the past few years has been recording operational losses.

To understand why, and to identify what could be done in response, a business evaluation was undertaken.

For this purpose, the following information was collected:

- **Financial statements**[1]**:** Ideally you should collect financial statements for the past three years, including the Profit & Loss Statement, Balance Sheet, Cash Flow Statement, and any budgets/forecasts available.[2] However, in Bundalong’s case, the business owners only had a Profit & Loss statement and Balance Sheet for the past two years; no cash flow statement and no budgets/forecasts.
- **Documented policies:** you should collect or create policies on key operational areas e.g. mark-up and pricing, procurement / buying, stock management, internal controls, staffing and rostering.
- **The organisation chart:** this should also include job descriptions
- **Compliance documents:** e.g. tax returns, bank loan agreements, leasing agreements and accreditation policies.
- **Industry information**[3]**:** which is both financial and industry-specific information, i.e. benchmarks.

Note: You may want to collect additional information, as is appropriate and available from your business, especially its business plan.

The following includes general guidance on different aspects of business evaluation and demonstrates the application of those principles using information from Bundalong.

FINANCIAL PERFORMANCE REVIEW

Start with evaluating the business’ current financial performance against its past performance. A comparative analysis such as this will shed light on trends which can be used to inform reactions to such trends. There are four main areas of financial performance that should be evaluated:

- Cash flow and liquidity
- Solvency
- Operating efficiency/productivity
- Profitability.

[1] Information from financial statements are historical. Thus, when analysing historical information, ensure the analysis is undertaken close to the preparation date to enhance the information’s utility.

[2] This should also include the assumptions that have been used to develop the budget

[3] When using financial information remember that there are a variety of accounting methods that can be applied to recording financial information. When performing comparisons, ensure the data has been prepared on the same basis for a meaningful comparison.

CASH FLOW AND LIQUIDITY

Cash is key when running a business so when you measure the success of your business, start with how much cash it is generating.

Cashflow forecast	The cashflow forecast is obtained by calculating opening bank balances plus all receipts for the period less all payments for the period. The period can be as short as weekly, however more commonly a cashflow forecast period is by month. Businesses experiencing cash flow difficulty should do their forecasting more frequently.
Description	A cashflow forecast is a very important tool for business as it provides information on future cash resources and how they will be applied to the business operations. Cashflow forecasting is an integral part of business planning and indicates any additional funding needs of the business in advance (so that the business can address such potential gaps).
Use	The forecast will predict the ability of your business to create the cash necessary for expansion or to support the operations of the business. It will also indicate any cashflow gaps the business may experience – periods when cash outflows exceed cash inflows.

In Bundalong's case, they had not prepared a cashflow forecast and therefore don't have good visibility of how much money is going in and out of the business.

Liquidity is the amount of cash and easily-convertible-to-cash assets a business owns to manage its short-term debt obligations. The three most common measurements for liquidity are the current ratio, the quick ratio (also known as the acid test) and the working capital to total sales.

Current ratio	$\frac{\text{Total current assets}}{\text{Total current liabilities}}$
Description	One of the most common measures of financial strength, the current ratio measures whether the business has enough current assets to meet its debts that fall due with a margin of safety.
Use	A generally acceptable current ratio is 2:1; however, this will depend on the nature of the industry and the form of its current assets and liabilities. For example, the business may have current assets made up predominantly of cash and would therefore survive with a relatively lower ratio.

Quick (acid) ratio	$\frac{\text{Total current assets less stock on hand}}{\text{Total current liabilities less bank overdraft}}$
Description	Quick (acid) ratio is one of the best measures of liquidity. By excluding inventories, which could take some time to turn into cash unless the price is discounted, this calculation concentrates on real, liquid assets.
Use	It helps answer the question: If the business does not receive income for a period, can it meet its current obligations with the readily convertible "quick" funds on hand? A quick ratio lower than 1.0 is a warning signal, as it indicates that current liabilities exceeds current assets.

Working capital to total sales	Total current assets less total current liabilities / Total sales
Description	Working capital to total sales provides an indication of how much working capital per dollar of sales the business should be holding.
Use	Analysis of this ratio must consider the type of trading the business is undertaking to provide any meaningful interpretation. For example, a business that sells a lot of low-cost items and cycles through stock quickly (such as a café) may only need 10 per cent to 15 per cent of working capital per dollar of sales. A manufacturer of heavy machinery and high-priced items with a slower stock turnover may require 20 per cent to 25 per cent working capital per dollar of sales.

BUNDALONG'S CASHFLOW AND LIQUIDITY MEASURES

	Cashflow forecast	Current ratio	Quick (acid) ratio	Working Capital to Sales ratio
Current year	No cashflow forecast recorded	1.64	0.54	0.12
Previous year		3.72	2.15	0.47

The ratios show that Bundalong's liquidity has deteriorated from the last year to the current year. It can be seen from the company's **balance sheet** that its real cash holdings have substantially decreased from $65,777 to $16,320. Based on the acid ratio, if the business does not sell its stock on hand, it may not be able to meet its current obligations.

SOLVENCY

Solvency ratios look at a business's ability to meet its debt obligations on an ongoing basis. The ratio looks at whether the business' assets or equity are sufficient to service its long-term debt. The gearing/leverage ratio is generally a good indicator of a business's long-term sustainability, measuring debt against owner's equity. A lower gearing ratio means that business operations are being financed by the owner and not creditors. What is considered an appropriate gearing ratio varies between industries but a downward trend over time is generally a good indicator that a business is on an increasingly solid financial ground. Lenders consider gearing ratios to help determine the borrower's ability to repay a loan.

Leverage (gearing) ratio	$\frac{\text{Total Liabilities}}{\text{Total Equity}} \times 100$
Description	The leverage (gearing) ratio indicates the extent to which the business is reliant on debt financing versus equity to fund the assets of the business. This ratio is widely used by lenders in banking covenants, therefore another reason to monitor this ratio is to ensure the business does not breach bank covenants. The degree of gearing reveals the level of financial risk the business faces. A highly geared or leveraged business is more susceptible to economic downturns. This is because the business must continue to meet its operational costs and pay off debts while income falls in challenging periods.
Use	The higher the ratio, the more difficult it will be to obtain further borrowings. A ratio of more than 50 per cent is typically considered a higher risk, although this is not a hard and fast rule.

Debt to asset ratio	$\frac{\text{Total Liabilities}}{\text{Total Assets}} \times 100$
Description	The debt to asset ratio measures the percentage of assets being financed by liabilities.
Use	This ratio should be less than 1, indicating adequacy of total assets to finance all debt.

BUNDALONG'S SOLVENCY MEASURES

	Leverage	Debt to Asset
Current year	69.55%	41.02%
Previous year	29.37%	22.68%

Bundalong is highly leveraged or geared, however to understand the risk of a 70 per cent gearing ratio, it is important to compare its gearing ratio to others in the same industry. For example, if its main competitor shows a gearing ratio of 75 per cent against an industry average of 80 per cent, Bundalong's 70 per cent ratio is less risky in comparison. In Bundalong's case however, a gearing ratio of 70 per cent is high for the plant nursery industry. This ratio is also impacted by Bundalong's continual losses.

The "debt to asset" ratio indicates that 41 per cent of the business's assets is financed by creditors and 59 per cent by the owners.

The ratio has nearly doubled from the previous year, indicating growing financial risk. Typically, businesses that are not very capital intensive are not expected to hold too much debt.

Managing debt levels is important and a safe gearing ratio can vary from business to business and is largely determined by how a business's debt is managed and how well the business is performing. In the case of Bundalong, looking at this ratio along with its liquidity ratio, shows that the company is not doing well. When you refer to the balance sheet in the **Appendix**, you notice the movement in the ratio is a result of a drop in profit.

To improve its gearing ratio Bundalong could consider:

- Profit improvement by cost minimisation
- Repaying long term loans
- Injecting more equity

IS DEBT FINANCING BAD?

Debt financing or use of leverage is not necessarily a 'red flag'. Debt can also help a company expand its operations, add new products and services and boost profits. Debt also reduces the amount shareholders need to invest in the business.

EVALUATING SOURCES OF FINANCE

When evaluating solvency, it is important to evaluate your sources of funding to ensure that your business will continue to have ready access to funding when required. In an evaluation of funding sources, you should check whether:

- you comply with your debt covenants
- you continue to meet the compliance requirements imposed by lenders e.g. reporting
- the debt facility is about to expire
- you have drawn down on the full finance facility or overdrawn on such facilities.

OPERATING EFFICIENCY/PRODUCTIVITY

As a business owner you should aim to achieve the best possible use of all business resources. Efficiency is about maximising the outputs of the business using the minimal level of inputs. Regular monitoring will ensure that the business is operating efficiently and that all assets are being used to generate the best return on investment.

Operating margin is the best indicator of operational efficiency. This metric provides an indication of how well the business is managing its costs. Inventory turnover is another good measure as it provides ongoing information about the effectiveness of your stock purchases. A successful business also needs engaged and productive employees executing goals aligned with your strategic objectives.

EMPLOYEE PRODUCTIVITY

Total sales to number of sales employees	$\dfrac{\text{Total Sales}}{\text{Number of sales employees}}$
Description	The total sales to the number of sales employees provides the average dollar value of sales made by sales employees for a period.
Use	Although this measure will only provide the average value of sales per employee, it is helpful in identifying trends.

Employee sales	Total value of sales made by each employee for the period.
Description	The employee sales measure is useful to review productivity of each employee.
Use	Although this measure will only provide the total value of sales per employee, it is helpful in determining how productive the business is in generating sales.

ASSET PRODUCTIVITY

Stock turnover	$\dfrac{\text{Cost of goods sold}}{\text{Average stock held for the period}}$ (average stock held for the period = opening + closing stock x 0.5)
Description	The stock turnover rate indicates the number of times the stock in the business has turned over.
Use	The lower the rate, the longer the stock is taking to turn over. This can provide an indication of issues with stock management, such as aged or excess stock holding. Funds that are invested in stock for longer periods can have an adverse impact on liquidity.

Total stock on hand to total assets	$\dfrac{\text{Total stock on hand}}{\text{Total assets}} \times 100$
Description	The total stock on hand to total assets ratio measures percentage of stock on hand included in the overall assets of the business.
Use	If a high percentage of a business's assets are tied up in stock and it does not have a relatively high turnover rate (a high turnover rate would be less than 30 days), it may be a signal that something is wrong and there could be potential for a stock write-down / off.

Debtor's days	$\dfrac{\text{Total debtors X number of days in the analysis period}}{\text{Total credit sales for the number of days in the analysis period}}$
Description	The debtor's days ratio indicates how promptly accounts from customers are being collected.
Use	When comparing the results of this calculation to the trade terms offered to customers, this will indicate slow paying customers as well as potential bad debts. The ratio is most useful when used in conjunction with an aged debtor's report.

Aged debtor's report	
Description	The aged debtor's report can be generated by a financial system that lists all outstanding customer payments by number of days. The list usually provides outstanding payments by current, 30 days, 60 days, 90 days and over.
Use	This report is particularly useful when used with the debtor's days calculation noted above. It will provide information on all outstanding customer accounts and can be used to chase up late payments and identify potential problem customer accounts.

Creditor's days	$\frac{\text{Total creditors X number of days in the analysis period}}{\text{Total cost of goods sold for the analysis period}}$
Description	The creditor's days ratio indicates how well accounts payable are being managed.
Use	When comparing the results of this calculation to the trade terms offered by suppliers, the results will provide information on supplier payments. If the analysis highlights that creditors are being paid on average before agreed payment terms cashflow can be impacted. If payments to suppliers are excessively slow, there is a possibility that supplier relationships may be damaged.

Aged creditor's report	
Description	The aged creditor's report can be generated by a financial system that lists all outstanding payments to suppliers by number of days. The list usually provides outstanding payments by current, 30 days, 60 days, 90 days and over.
Use	This report is particularly useful when used with the creditor's days calculation noted above. It will provide information on all outstanding supplier accounts and can help when preparing forecasted cash payments.

CAPITAL EFFECTIVENESS

Total asset turnover	$\frac{\text{Total sales}}{\text{Total assets}}$
Description	The total asset turnover measures the ability of a business to use its assets to generate sales.
Use	The lower the total asset turnover ratio, as compared to historical data for the business and industry data, the more sluggish the business sales are. This may indicate a problem with one or more of the asset categories composing total assets – stock, debtors or fixed assets. Each asset class should be reviewed to determine where a potential problem may lie.

Return on assets (ROA)	$\frac{\text{Net profit before tax}}{\text{Total assets}} \times 100$
Description	The total asset turnover measures the ability of a business to use its assets to generate sales.
Use	The lower the total asset turnover ratio, as compared to historical data for the business and industry data, the more sluggish the business sales are. This may indicate a problem with one or more of the asset categories composing total assets – stock, debtors or fixed assets. Each asset class should be reviewed to determine where a potential problem may lie.

Return on equity/ investment (ROI)	$\frac{\text{Net profit before tax}}{\text{Total assets}} \times 100$
Description	The ROI is perhaps the most important ratio of all as it tells you whether or not the effort put into the business is returning an appropriate return for the business owner/s, in addition to achieving the strategic objectives.
Use	If the ROI is less than the rate of return on low risk investments, such as a term deposit, this raises the question of the overall investment in this business.

EFFICIENCY AND EFFECTIVENESS OF POLICIES AND PROCESSES

In addition to these financial measures of efficiency, you should also review the efficiency and effectiveness of your policies and processes.

To help you identify where improvements can be made, you'll need to understand the strengths and weaknesses of your current processes and document how things should be done. Start by working with your staff to document the processes behind each task, step by step.

Ask someone in your business who has never completed the task to test the process. Is the process seamless? Are any steps missing? Are there any unnecessary steps? Is there a better way of doing it?

Test the process yourself. Ask yourself, do those processes support your business strategy? If yes, sign off on it, if not change the process.

Examples of key policies to review or develop include (but are not limited to):

- mark-up policies
- discount policies
- expenditure policies (such as travel policy, vehicle policy, personnel policies)
- authorisation policies (such as budget approval policy)
- internal control policies (such as staff sales policies)

BUNDALONG EFFICIENCY MEASURES

	Stock turnover (Benchmark: 3.5)	Total stock on hand to total assets	Debtors' average days outstanding	Creditors' average days outstanding	Total asset turnover	Return on assets (ROA)	Return on equity (ROI)	Total sales to sales employees
Description	2.30	39.58%	21	58	1.79	Nil	Nil	$109,676
Use	1.73	34.02%	58	182	0.98	Nil	Nil	$98,661

Bundalong's stock turnover rate provides some indication of stock issues, with the current year rate approximately 33 per cent below the plant nursery benchmark. When considering a retail nursery, stock will be bought to sell according to season in addition to a standard "year-round" stock. It's not surprising with four seasons and some annual stock that the industry stock turnover rate is 3.5.

Debtor's sales on average for the current year were 58 per cent of total sales. This indicates a higher than average reliance on trade sales (as opposed to retail sales), with the benchmark for retail nurseries in non-metro towns of 25 per cent. However, with average debtors' days outstanding of 21 days, this may not be such an issue as collections appear in order.

It may however indicate there is room to grow retail sales, which could improve cashflow as such customers typically pay at the point of purchase.

Creditor's days of 58 days indicate slow payment to suppliers, as average terms are 30 days. This could indicate issues with cashflow and highlights the need for a cashflow forecast to be developed and maintained. This view is supported by the total stock on hand as a percentage of current assets at 40 per cent for the current year. This could lead to cashflow issues where short term debts need to be paid.

While no metric is recorded, the return on assets and equity are impacted by the continual losses.

PROFITABILITY

While some businesses can survive for some time without being profitable, to survive in the long run, a business must eventually attain and maintain profitability.

The best metric for evaluating profitability is net margin. Evaluating profitability can also be undertaken by using other profitability ratios, return ratios and using the mark-up and break-even calculations as set out below:

Net profit margin	$\frac{\text{Net profit}}{\text{Total sales}} \times 100$
Description	The net profit margin is calculated using the net profit after tax and interest (EBIT) and includes any other non-trading income.
Use	This measure should be used to compare the overall results of the business against other time periods. In deciding which periods should be used in the comparison, the type of business should be considered. For example, when analysing a seasonal business, such as a snow skiing equipment store, it would be more useful to compare the winter season of the current year with the winter season of the previous year rather than comparing the previous month with the current month. Also, use this metric for an industry comparison. A larger net margin, when compared to the industry average, indicates your business has a greater margin of financial safety and is in a better financial position to commit capital to growth and expansion.

Gross profit margin	$\frac{\text{Gross profit}}{\text{Total sales}} \times 100$
Description	Gross profit margin is the percentage of sales dollars remaining to pay general expenses following the deduction of the cost of goods sold. Cost of goods sold can include direct costs, such as materials / merchandise costs, carriage inwards on these, processing costs and production overheads.
Use	Analysis of this margin will assist in assessing the efficiency of the business, including the efficiency of pricing, stock purchasing procedures and handling. Well-designed and executed processes keep costs low and increase the gross margin.

Mark-up	$\frac{\text{Gross profit}}{\text{Cost of goods sold}} \times 100$
Description	Mark-up is the percentage difference between the actual cost and the selling price.
Use	It is generally only a meaningful figure when referring to the sale of products rather than services. It can be useful to use the mark-up calculation to ensure you set the selling price at a level that covers all costs incurred with the sale.

Earnings before interest and tax (EBIT) margin	$\frac{\text{Net profit before interest and tax}}{\text{Total sales}} \times 100$
Description	This EBIT margin is the percentage of sales dollars left after deducting the cost of goods sold and all expenses, except income taxes.
Use	This measure enables the business to accurately compare the profit results with other businesses in the same or similar industries. Interest and tax are excluded as tax and interest can vary for each business. The analysis will provide information on the return on sales of the business. This ratio is often quoted by analysts reviewing the performance of a business compared to other businesses in the industry.

Break even analysis	$\frac{\text{Fixed expenses}}{\text{1 less (cost of goods sold)/(Total sales)}}$
Description	The break-even calculation shows how many sales have to be made in dollar terms before all the expenses are covered and actual profit begins.
Use	This measure provides information on the correlation between sales, volume and price. It is particularly useful for setting sales targets for the business or employees. Once the break-even figure is known, then the business can monitor sales to ensure that all expenses for the period will be covered.

BUNDALONG PROFITABILITY MEASURES

	Gross profit margin	Mark-up	Earnings before interest and tax (EBIT) margin	Net profit margin
Description	43.37%	76.58%	(29.39%)	Same as EBIT – no tax paid due to losses
Use	52.03%	108.46%	(33.96%)	

Gross margin for current year has decreased from the previous year and is 7.6 per cent below benchmark data. Given that there has been a substantial increase in sales, it appears that this reduction will be mainly due to stock issues.

SUMMARY OF FINANCIAL PERFORMANCE REVIEW

There is no single metric that can identify the overall financial and operational health of a business. Liquidity tells you about Bundalong's ability to ride out short term rough patches; solvency tells Bundalong whether it can readily cover long-term debt obligations; and efficiency and profitability gives an indication on Bundalong's ability to convert inputs into cash flow and income. All these factors together are necessary to get a complete and holistic view of the business's financial performance.

In the case of Bundalong, comparisons of metrics between current and previous year, as well as industry benchmark, points towards cash flow, stock and cost management issues. To understand the reasons and identify "next steps", further investigation was required.

Had the metrics of Bundalong indicated that the business was stable and tracking well, a further investigation into "what works" and "what can be done better" is still advisable to ensure continuous improvement and to build/exploit its competitive advantage.

DEEPER INVESTIGATION

Stock turnover analysis

A deeper investigation into stock management at Bundalong was found necessary because the 76.6 per cent mark-up rate for the current year was:

- below the industry benchmark
- well down from the mark up rate of 108.5 per cent in the previous year
- well below the business's mark up policy rate of 110 per cent.

The deeper investigation of stock management found:

- Although the mark-up on stock was adjusted twice during the current year to reflect higher purchase price of goods, further analysis into the decrease in gross margin highlighted an increase in freight charges. Total freight and potting charges (add on costs) amount to $17,001, approximately 7 per cent of total cost of goods sold during current year. These charges had not been accounted for in the final selling price and account for most of the decrease in gross margin. The retail plant nursery association confirmed that increasing freight costs were being experienced across the industry in the past 12 months.
- Included in the cost of goods sold is the amount of stock "written off" during the year. This is recorded as "destroyed stock" and unaccounted losses realised at stocktake. The current procedure for "destroying" stock is that any staff member can identify stock which is dead or not in a sellable form at any time. The owner has advised that at one stage this procedure had to be approved by the owner, however this is not currently being adhered to. To record destroyed stock, the item is sold to the "destroyed stock" account and the plant and pot is disposed of. At the end of each month, the closing stock balance is adjusted to reflect the destroyed stock. There is currently no review of destroyed stock, either physical or in regular reports. There is a brief reference to destroyed stock in the general procedures and instructions on how to record destroyed stock. Further analysis of destroyed stock found that 15 per cent of all destroyed stock was recorded on weekends, when there is no management supervision.
- Following the current year stocktake, records show that a further $16,523 of stock was missing from the physical count, representing 6.6 per cent of the total cost of goods sold. The closing stock balance for the current year was reduced by this amount to record this loss or shrinkage.

- Taking account of the destroyed stock and stock losses realised during the current year stocktake, the total shrinkage of stock at cost price amounted to $28,813 or 11.65 per cent of total cost of goods sold and 27 per cent of the average stock holdings for the current year. Consultation with the industry association indicated that destroyed stock should average approximately $4000 (at cost) per annum based on the total sales of Bundalong.

Therefore, destroyed and stock losses are well in excess of industry standards. If the destroyed or lost stock is added back to the profit and loss statement, it leaves the following different:

	Current figures	Adjusted figures
Mark-up	76.59%	99.76%
Stock turn	2.30	1.79

- The average stock holdings for the current year was $122,641 (including stock losses). The average level of stock holdings required to meet benchmark stock turn, where cost of goods remain the same, is $63,008. A physical analysis on aged stock was undertaken by the owner (currently the stock management software system does not allow for specific data on aged stock). Aged stock (held for more than six months) was estimated at approximately $31,783. In the event that the aged stock had been sold, the average stock levels would decrease to $90,857 (giving a stock turn rate of 2.41 turns), bringing it somewhat closer to the industry benchmark.
- Low stock turnover rate can lead to higher probability of destroyed stock and /or aged stock. It also limits the ability of Bundalong to purchase new stock due to space constraints. This in turn could result in lower sales due to lower than acceptable levels of "fresh" stock.
- Bundalong was also found to have no formal buying procedure. Currently, stock purchases are decided through discussions with staff. Details of stock movement, such as stock at low levels, high turnover and plants that customers have requested, is provided by staff. This, together with seasonal requirements, forms the basis for purchase. The informal nature of the buying procedure could account for the high level of stock holdings, excess stock and hence destroyed stock. A formal buying policy would include analysis of current stock to ensure that stock turn and average stock holdings are in line with agreed benchmarks.
- Given the level of information held in the current stock management system, it is possible that this data can be used to assist in the buying procedures. Information on high volume of sales of certain stock items, stock held past a certain time frame and low levels of stock items should form part of the formal buying procedures.

To improve stock turnover and gross margin, Bundalong should consider:

1. Reducing average stock levels.
2. Monitoring and managing ageing stock.
3. Implementing policy for destroying stock.
4. Regularly monitoring mark-up to ensure all costs are covered in selling price.
5. Develop and implement a formal buying procedure.

Sales Analysis

Total sales for current year increased by 27 per cent to $438,707 compared to previous year total sales of $345,314.

Detailed analysis of sales records (point of sale) provided the following information:

- Thirty-six per cent of all sales were achieved in three trading months; August, September and December. The analysis also indicated that approximately 30 per cent of sales were achieved in the slowest five months of the current year.
- An analysis of the overall sales as a percentage achieved for each day of the week highlighted that trading on Saturday and Sunday generated 36 per cent of total sales (public holidays have been included in the trading figures for Sunday). The review noted that for most weekends and public holidays, staffing levels were two full- time equivalents (FTE) with no supervision from the owner.
- The official trading hours for the retail operation is 59.50 hours per week (8.30am to 5.00pm, including weekends). When compared to the benchmark data, this is a high number of trading hours, however, it is within an acceptable range.
- The sales records also show that 86 per cent of overall sales (on average) are completed after 11.00am each day.
- The total amount of discount applied during the current year was $41,158 (9.4 per cent of total income). No comparison to the previous year was conducted as discount amounts were not separately recorded.
- Two competitors were "mystery shopped" to ascertain the discount policies they offer. It appears that the Bundalong discount policy is extremely generous. With 58 per cent of sales made to account customers (landscapers and other larger organisations) and the same customers receiving the most beneficial discounts, the discounting policy is having a significant impact on total income.
- The profit and loss statement was adjusted to reflect "add backs" of discounting and destroyed and unaccounted for stock losses to show the difference:

	Current year		With stock adjustments and discounts removed	
	$	**% of sales**	**$**	**% of sales**
Sales	438,707		479,865	
Cost of goods sold				
Opening stock	119,979		119,9790	
Purchases	224,938		224,938	
	344,917		344,917	
Closing stock	(96,490)		(125,303)	
Total cost of goods sold	248,426	56.6%	219,613	45.8%
Gross profit	**190,280**	**43.4%**	**260,251**	**54.2%**
Operating expenses				
Salaries	(233,294)	53.2%	(233,294)	48.6%
Overheads	(85,903)	19.6%	(85,903)	17.9%%
Total operating expenses	(319,198)	72.8%	(319,198)	66.5%
Net profit/loss	**(128,917)**		**(58,946)**	

Potential action points noted for Bundalong:

1. Record discounts separately in profit and loss statement against sales.
2. Amend discount policy.
3. Review pricing structure including mark-up policy.
4. Review staff roster for weekends to maximise sales potential.

OTHER FACTORS TO CONSIDER IN YOUR SALES ANALYSIS

As an extension to a sales analysis, consider:

1. How effectively are you meeting customer needs with the goods and/or services you offer?
2. How effectively are you matching your goods and services to your customers' needs?
3. Which of your products and services are succeeding? Which aren't performing as planned? Decide which products and services offer both a high percentage of sales and high profit margins.
4. What's really behind issues with a product or service, such as a high number of complaints? Consider areas such as pricing, marketing, sales and after-sales service, design, packaging and systems during your review. Look for "quick wins" that give you the breathing space to make more fundamental improvements.
5. Are you reviewing costs frequently? Are you keeping a close eye on your direct costs, your overheads and your assets? Are there different ways of doing things or new technologies you could use that would lower your costs? Consider ways in which you can negotiate better deals with your suppliers.

Cost management: overhead expenses analysis

In comparison to the industry benchmark, Bundalong's level of salary costs as a proportion of income is high. Salary expense for the current year was $233,294 (53.2 per cent of sales) compared to $200,236 (58.0 per cent) in the previous year and the industry benchmark of 20 to 25 per cent.

Due to this large difference between the salary costs of Bundalong and the industry benchmark, a deeper review of productivity and staff rostering was undertaken. This review provided the following observations:

- Bundalong have 5.3 full time equivalent (FTE) staff compared to the benchmark of a similar business of 4.2 FTE.
- Sales to hours paid showed the January to June period was less productive than the July to December period (which included the top three months for sales):
  - Full current year per hour paid $39.10 sales
  - July to December per hour paid $46.33 sales
  - January to June per hour paid$31.90 sales
- A review of the annual sales percentage per day and number of rostered staff clearly showed that the two highest days in sales (weekends) have the lowest staff in attendance.
- Advertising expense is significantly higher than the benchmark data for both current and previous year. Given that the total income is in line with benchmark data, this indicates that promotion is not effectively translating to additional income.

- Vehicle operating costs for both current and previous year are lower than benchmark.
- The sales records also show that 86 per cent of overall sales (on average) are completed after 11.00am each day.
- The total amount of discount applied during the current year was $41,158 (9.4 per cent of total income). No comparison to the previous year was conducted as discount amounts were not separately recorded.
- Two competitors were "mystery shopped" to ascertain the discount policies they offer. It appears that the Bundalong discount policy is extremely generous. With 58 per cent of sales made to account customers (landscapers and other larger organisations) and the same customers receiving the most beneficial discounts, the discounting policy is having a significant impact on total income.
- The profit and loss statement was adjusted to reflect "add backs" of discounting and destroyedand unaccounted for stock lossesto show the difference:

Potential action points:

1. Develop position descriptions for all staff positions.
2. Restructure staffing levels and responsibilities.
3. Review salary expenses and bring in line with benchmark data.
4. Implement staff accountabilities through key performance indicators for each staff member to monitor productivity.
5. Monitor and manage staff roster.
6. Review advertising, and consider advertising spend that can be monitored for success.

OTHER AREAS OF REVIEW

OTHER AREAS OF REVIEW:

Identify other areas for review based on your answer to these questions:

- What's my direction?
- Looking at where you are now, where do you want to go over the next three to five years and how you intend to get there?
- What are my markets - now and in the future?
- Consider which markets you should / want to compete in: how will they change and what does the business need in order to be involved in these markets?
- How do I gain market advantage?
- Identify your competitors and look at what your business can do better than its competition in the chosen markets?

Sales of applied stock – growth potential

The owners of Bundalong wanted to understand how applied stock e.g. fertiliser (i.e. not their plants) contributed to overall profitability. Understanding this will inform their decision of selling more applied stock and seeking alternative revenue streams. This is particularly important as applied stock can often carry higher gross margin.

From their accounts it was identified that applied stock sold in the current year was $18,043 (4.1 per cent of sales), well below the industry standard of 30 to 35 per cent. This implies that there is a bigger opportunity for Bundalong to sell their applied stock. It therefore needs to review its strategy for selling these complementary products.

Cash handling process – internal controls

- Bundalong had a policy that one person is to cover the cash register activity each day. However, based on a review of the customer transaction reports, it appears this policy was often breached, especially on weekends when only two staff members are working. Bundalong will need to review the practicality of this policy when a large proportion of its sales are generated on the weekend.
- End-of-day cash register sales tallies are prepared by the person responsible for the daily register duties. However, there is no policy in place for a second review. Although in practice if the tally sheet does not balance a second person will review it, the overall practice creates a high risk as the person responsible for the collection of cash from sales is also responsible for end of day cash reconciliation. There is therefore a possibility that a sale may not be entered through the register, or voided, or entered as returned and the cash not entered in the register. Should there be any such event, it would be difficult to detect it under the current procedures.
- A review of the customer transaction report also indicated that on many occasions staff were processing sales to themselves (staff sales). This should not occur, especially without supervision. Bundalong will need to institute controls that always require staff sales to be processed by the owner or a senior manager on duty.

Potential action points:

1. Train staff to “up-sell” applied stock to increase margins.
2. Amend and document cash register responsibilities.
3. Review all internal control processes, with particular emphasis on controls over stock to avoid shrinkage.
4. Train staff on the importance of adhering to internal control processes.

CONCLUSION

When evaluating business performance, look at:

- **Core activities:** What do you do, the products you make or services you provide? What makes them successful, how could they be improved, and could you launch new complementary products or services?
- **Cash flow and liquidity:** Set up a cash flow forecast and regularly review and update the forecast. This is the balance of all the money flowing in and out of your business.
- **Working capital:** Compare with past performance and against other businesses in your industry Consider whether your requirements have changed and why there are movements? Do you need to source additional capital?
- **Cost base:** Constantly review your cost base and ensure the costs are covered in your sale price, but don't expect customers to pay for business inefficiencies.
- **Borrowing and growth:** What line of credit or loans do you have? Are there more appropriate or cheaper forms of finance you could switch to instead? Do you have plans in place to adapt your financing to accommodate your business' changing needs and growth?
- **Operating efficiency and productivity:** As a business owner you should aim to achieve the best possible use of all business resources. Efficiency is about maximising the outputs of the business using the minimal level of inputs. Regular monitoring will ensure that the business is operating efficiently, that all assets are being utilised to generate the best return on investment, and staff are productive.

A good business performance evaluation looks beyond the numbers to non-financial drivers such as customer base / market segmentations to understand what makes your offerings successful, how they could be improved and if there's an opportunity for selling complementary products or services.

If the business evaluation highlights areas of concern, investigate in greater depth. If the review highlights areas where your business outperforms other areas, also investigate that as you may pick up lessons for other areas of your business.

Once you have evaluated the business performance (including reviewing against benchmark data from your industry), revisit and update your business plan. Make sure you include the developments you've noted in your evaluation.

APPENDIX A: BUNDALONG'S FINANCIAL & OPERATIONAL DATA

FINANCIAL STATEMENTS OF BUNDALONG RETAIL NURSERY PLANT

Profit and loss statement* for year ended July

	Current year		Previous year	
	$	% of sales	$	% of sales
Sales	438,707.15		345,314.93	
Cost of goods sold				
Opening stock	119,979.00		71,573.65	
Purchases	224,938.00		214,050.11	
	344,917.00		285,623.76	
Closing stock	(96,490.49)		(119,979.00)	
Total cost of goods sold	248,426.51	56.63%	165,644.76	47.97%
Gross profit	**190,280.64**	**43.37%**	**179,670.17**	**52.03%**
Operating expenses				
Salaries	(233,294.80)	53.18%	(200,236.01)	57.99%
Overheads	(85,903.42)	19.58%	(96,691.18)	28.00%
Total operating expenses	(319,198.22)	72.76%	(296,927.19)	85.99%
Net profit/loss	**(128,917.58)**		**(117,257.02)**	
Average stock held for each year	$ 108,234.75		$ 95,776.33	

*Profit & Loss Statement / Income Statements measure the profitability of your business during a certain time period by showing your business's profits and losses.

Breakdown of operating expenses

Operating expenses	Current year		Previous year	
	$	% of sales	$	% of sales
Cleaning contract	1,740.00	2.03	1,160.00	1.20
Repairs and maintenance				
Buildings	794.26	0.92	656.39	0.68
Equipment	978.22	1.14	859.64	0.89
Furniture and fittings	1,702.80	1.98	1,626.81	1.68
Grounds	4,656.30	5.42	9,646.20	9.98
Electricity	2,821.48	3.28	2,729.10	2.82
Vehicles				
Fuel	3,220.07	3.75	2,578.55	2.67
Registration	355.00	0.41	352.20	0.36
Insurance	1,250.00	1.46	1,200.00	1.24
Repairs and maintenance	1,712.51	1.99	1,872.71	1.94
Transport – contract	—	—	460.04	0.48
Depreciation				
Equipment	5,152.84	6.00	5,421.84	5.61
Furniture and fittings	4,324.41	5.03	4,961.39	5.13
Motor vehicles	6,392.29	7.44	6,577.53	6.80
Advertising	14,515.12	16.90	15,954.60	16.50
Uniform costs	277.89	0.32	451.54	0.47
Printing and stationery	1,017.50	1.18	892.62	0.92
Telephone	2,655.50	3.09	2,960.61	3.06
Staff provisions	1,431.55	1.67	1,665.49	1.72
Rent	22,455.00	26.14	19,525.00	20.19
Equipment	620.00	0.72	1,222.22	1.26
Staff training	310.09	0.36	438.18	0.45
Traveling	191.07	0.22	76.63	0.08
Materials and supplies	529.48	0.62	581.65	0.60
Bank charges	3,013.19	3.51	2,809.30	2.91
Memberships and subscriptions	579.32	0.67	520.00	0.54
Health and safety	259.30	0.30	117.79	0.12
Postage	364.70	0.42	369.44	0.38
Computers	—	—	4,504.14	4.66
Sundry administration costs	2,583.53	3.01	1,681.39	1.74
Consultancy fees	—	—	2,818.18	2.91
Total operating expenses	**85,903.42**		**96,691.18**	

Areas noted for further review from figures above include decrease in ground maintenance expense, increases in rent, bank charges and why there is no computer expense for the current year (i.e. is technology not up to date?).

Balance sheet*

	Current year	Previous year
	$	$
ASSETS		
Current assets		
Cash/bank	16,320.00	65,777.82
Debtors	14,280.00	32,000.00
Stock	96,490.00	119,979.00
Other	4,210.00	5,500.00
Total current assets	**131,300.00**	**223,256.82**
Non-current assets		
Delivery vehicle	75,000.00	75,000.00
Less accumulated depreciation	(19,547.35)	(12,969.82)
Total	55,452.65	62,030.18
Nursery fit out	115,000.00	115,000.00
Less accumulated depreciation	(66,955.45)	(61,994.06)
	48,044.55	53,005.94
Equipment	50,000.00	50,000.00
Less accumulated depreciation	(41,021.20)	(35,599.36)
	8,978.80	14,400.64
Total non-current assets	112,476.00	129,436.76
Total assets	**243,776.00**	**352,693.58**
LIABILITIES		
Current liabilities		
Creditors	65,000.00	48,000.00
Credit card	15,000.00	12,000.00
Total current liabilities	80,000.00	60,000.00
Non-current liabilities		
Bank loan	20,000.00	20,000.00
Total liabilities	**100,000.00**	**80,000.00**
EQUITY		
Shareholders' funds (including retained earnings, losses)	272,693.58	389,950.60
Less current year accumulated losses	(128,917.58)	(117,257.02)
Total equity	**143,776.00**	**272,693.58**

*Balance Sheet shows your business's financial health, measuring how much you owe and own.

Areas noted for further review from figures above include increases in current liabilities, no finance facility in place (contingency plan), substantial decrease in cash at bank.

OPERATIONAL INFORMATION OF BUNDALONG RETAIL NURSERY PLANT

Operational activities

Staffing	
FULL-TIME EQUIVALENT	5.30, INCLUDING:
Owner / manager	1.30
Apprentice	1.00
6 Part-time	3.00
PART-TIME DUTIES INCLUDE:	
General sales, orders, quotes	0.80
General sales, admin	0.60
General sales, buying	0.60
General sales	0.60
2 staff general sales (2 x 0.20)	0.40
Trading hours: 59.50 hours per week, 8.30am to 5.00pm every day except major public holidays.	

Documentation reviewed

Mark-up policy:	The standard mark-up policy is 110 per cent.
Buying policy:	No formal buying policy held.
Job descriptions:	No formal job descriptions held.
Discount/VIP policy:	The discount policy notes the following:

Discount	Category
2.5%	• Non-VIP members
10%	• VIP members • Schools • Businesses • Garden design customers
15%	• Landscapers value to $200
20%	• Landscapers value $201 to $500 • TAFE and other colleges
25%	• Landscapers value more than $500 • Nursery staff

INDUSTRY BENCHMARK

As provided by Bundalong retail plant nursery from their industry association.

Financial benchmarks	
Total average income	$ 446,556
Cost of goods sold	48.99%
Gross margin	51.01%
SELECTED OVERHEADS AS PERCENTAGE OF INCOME	
Advertising and promotion	2.26%
Salaries and wages including staff on costs	13.77%
Vehicle operating costs	3.74%
Rent	3.32%
Bank charges	1.53%
Total overheads	37.25%
Net profit margin	13.76%
PERSONNEL NUMBERS (FTE)	
Working owners	1.52
Sales staff and nursery people	2.36
Any other staff	0.49
Total personnel	4.37
OTHER BENCHMARK INFORMATION	
Stock turn rate	3.50
Plants grown in house as percentage of total sales	20.00%
Trading hours per week	54
Percentage of sales made to account customers	25.00%

Analysis of Bundalong retail nursery financial information in comparison to the benchmark in current and previous year

	Industry benchmark	Bundalong current year	Variance of current year to benchmark	Bundalong previous year	Variance of current to previous year	Variance of previous year to benchmark
	$446,556.00	$438,707.15	($7,848.85)	$345,314.93	$93,392.22	($101,241.07)
Cost of goods sold	48.99%	56.63%	7.64%	47.97%	8.66%	(1.02%)
Gross margin	51.01%	43.37%	(7.64%)	52.03%	(8.66%)	1.02%
SELECTED OVERHEADS AS A PERCENTAGE OF INCOME						
Advertising and promotion	2.26%	16.90%	14.64%	16.50%	0.40%	14.00%
Salaries including staff on costs	13.77%	53.18%	39.41%	57.99%	(4.81%)	44.22%
Vehicle operating costs	3.74%	7.61%	3.87%	6.21%	1.40%	2.47%
Rent	3.32%	26.14%	22.82%	20.19%	5.95%	16.87%
Bank charges	1.53%	3.51%	1.98%	2.91%	0.60%	1.38%
Total overheads	37.25%	72.76%	35.75%	85.99%	(13.00%)	48.75%
Net profit margin	13.76%	(29.39%)	(43.15%)	(33.96%)	4.57%	(47.72%)
PERSONNEL NUMBERS (FTE)						
Working owners	1.52	1.30	(0.22)	1.30	0	(0.22)
Sales staff and nursery people	2.36	4.00	1.64	3.50	0.50	1.14
Any other staff	0.49	0	(0.49)	0	0	(0.49)
Total personnel	4.37	5.30	0.93	4.80	0.50	0.43
OTHER BENCHMARK INFORMATION						
Stock turn rate	3.50	2.30	(1.20)	1.73	0.57	(1.77)
Plants grown in house as a percentage of total sales	20.00%	22.00%	2.00%	20.00%	2.00%	0
Trading hours per week	54	59.50	5.50	59.50	0	5.50
Percentage of sales made to account customers	25.00%	58.00%	33.00%	55.00%	3.00%	30.00%

Commentary on industry benchmark variances

Total income	The total income in the current year is up from the previous year and is within 5 per cent of industry benchmark.
Cost of goods sold	Total cost of goods sold for the current year is 8.66 per cent higher than the previous year and 7.64 per cent higher than the benchmark. ***Recommend further investigation.***
Gross margin	Gross margin variances in line with cost of goods sold variances noted above. Review cost of goods sold.
Selected overheads as percentage of income	
Advertising and promotion	Current year expense up slightly from previous year. This expense for current year and previous year are substantially higher than benchmark. ***Recommend further investigation.***
Salaries including staff on costs	Current year expense lower than previous year, although increase in staff numbers (see FTE data below). However, figures are still substantially higher than benchmark. ***Recommend further investigation.***
Vehicle operating costs	This expense for both current and previous year is higher than the benchmark. ***Recommend further investigation.***
Total overheads	Current year expenses lower than previous year, however substantially higher than benchmark most likely due to high salary overheads. ***Recommend further investigation.***
Net profit margin	Net operating loss reported for both current and previous year due to key areas noted above.
Personnel numbers (FTE)	
Working owners	The owner is working slightly below benchmark.
Sales and nursery staff	The current year staffing is higher than previous year (although overall salaries are lower) and higher than benchmark data. ***Recommend further investigation.***
Any other staff	
Total personnel	
Other benchmark information	
Stock turn rate	The current year stock turn rate is higher than the previous year, however, both figures are well below benchmark. ***Further investigation recommended.***
Plants grown in house as percentage of total sales	The current year plants grown in house is higher than benchmark. ***Further investigation recommended.***
Trading hours per week	Total trading hours remained constant for both current and previous year, and slightly higher than the benchmark.
Percentage of sales made to account customers	The percentage of sales made on account increased slightly in current year compared to previous year, however for both years this percentage is substantially higher than industry benchmarks. Given these sales are on discount, it means that most sales are below the mark-up stated in the mark-up policy. ***Further investigation recommended.***

APPENDIX B: CHECKLIST OF SUGGESTED INFORMATION SOURCES FOR BUSINESS EVALUATION

STRATEGIC	• One and five-year strategic plans • Succession plan
FINANCIAL INFORMATION	• Financial statements – profit and loss, balance sheet • Current year budget • Current year forecast – profit and loss and cashflow • Point of sale information – sales by employees, goods returns, no sale items and other relevant information • Stock management records • Work-in-progress records and reports
COMPLIANCE REPORTING	• Taxation returns, including goods and services tax statements if required • Loan, lease and other financing agreements • Accreditation reports • Financial statements • Industry-specific reports
POLICIES AND PROCEDURES	• All human resources policies, including job descriptions, organisation charts and staff rosters • All financial policies, including pricing, discounting and buying • Internal control procedures, such as segregation of duties • Disaster and emergency planning policies, including data back-up
PHYSICAL ASSESSMENT	• Review controls in place, such as security cameras, security of stock, security of passwords and other access methods

APPENDIX C: EXAMPLE OF A TEMPLATE FOR BUSINESS EVALUATION

Analysis of industry benchmark to current and previous year

	Industry benchmark	My business' current year	Variance of current year to benchmark	My business' previous year	Variance of current to previous year	Variance of previous year to benchmark
Total income						
Cost of goods sold						
Gross margin						
SELECTED OVERHEADS AS A PERCENTAGE OF INCOME						
Advertising and promotion						
Salaries including staff on costs						
Vehicle operating costs						
Rent						
Bank charges						
Insert other key overheads for the business						
Net profit margin						
PERSONNEL NUMBERS (FTE)						
Working owners						
Sales staff						
Any other staff						
Total personnel						
OTHER BENCHMARK INFORMATION						
Stock turn rate						
Trading hours per week						
Insert other key benchmark information for the business						
Percentage of sales made to account customers						

Profitability measures

	Formula	Current Year	Previous Year	Benchmark	Comment
Gross profit margin	Gross profit / Net sales x 100				
Mark-up	Gross profit / Cost of goods sold x 100				
Earnings before interest and tax (EBIT) margin	Net profit before interest and tax / Net sales x 100				
Net profit margin	Net profit / Total Income x 100				
Break even analysis	Fixed expenses / 1 less (cost of goods sold)/(net sales) x 100				

Cash flow, liquidity and solvency measures

	Formula	Current Year	Previous Year	Benchmark	Comment
Working capital to total sales	Total current assets less total current liabilities / Total sales				
Current ratio	Total current assets / Total current liabilities				
Quick (acid) ratio	Total current assets Net sales / less stock on hand Total current liabilities less bank overdraft				
Leverage (gearing) ratio	Total liabilities / Total equity				
Debt to asset ratio	Total liabilities / Total assets				

Cashflow forecast	Opening bank balances plus all receipts for the period less all payments for the period. The period can be as short as weekly, however, more commonly a cashflow forecast period is for a month. For businesses experiencing cash flow difficulty, it is recommended that forecasting is done more regularly than what is usual for the business.	Comments

Evaluation of funding sources	Review all loan documentation and finance facilities (such as overdrafts), including leases, hire purchase and debtor finance and ensure that each finance facility is readily available when required. Areas of review should include loan terms and conditions and financial covenants and reporting compliance requirements.	Comments

Efficiency measures

	Formula	Current Year	Previous Year	Benchmark	Comment
Stock turnover	Cost of goods sold / Average stock held for the period				
Total stock on hand to total assets	Total stock on hand / Total assets				
Debtor's days	Total number of days in debtors X the analysis period / Total credit sales for the analysis period				
Creditor's days	Total number of days in creditors X the analysis period / Total cost of goods sold for the period				
Total asset turnover	Net sales / Total assets				
Return on assets (ROA)	Net profit before tax / Total assets				
Return on equity/ investment (ROI)	Net profit before tax / Total equity				
Total sales to number of sales employees	Total sales / Number of sales employees				

Employee sales - Total value of sales made by each employee for the analysis period	Current year	Previous year	Variance	Comments
Employee 1				
Employee 2				
Employee 3				

Aged debtors report*	Current year	Previous year	Variance	Comments
Current				
31 to 60 days				
61 to 90 days				
91 to 120 days				
121 days >				

*Attach financial system report to provide detail on each customer. The terms in report should match terms provided to customers

Aged creditors report*	Current year	Previous year	Variance	Comments
Current				
31 to 60 days				
61 to 90 days				
91 to 120 days				
121 days >				

*Attach financial system report to provide detail on each customer. The terms in report should match terms provided by suppliers