Business Overview Report

Version 1.0 – 1 of 1 (B)

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The Business Overview Report - Purpose

The Business Overview Report is a concise but incredibly valuable financial analysis report provided on two pages comprising:

- **Your client's financial history, but bang up to date**
  - ✓ An overview of their profit (loss), and it's constituent parts
  - ✓ The last month, quarter and year compared to last year
  - ✓ Net worth movement in the last month, quarter and year
- **Key sales drivers, (transactions and value)**
- **Key customer drivers, (acquisition and attrition)**
- **Current Ratio, Debtor and Creditor Days**

You can use the Business Overview Report to get a quick and thorough overview of your client's financial performance and more important, understand the impact of the movement in their key sales drivers over the last two years.

You cannot do anything to change the history, that has already happened, but seeing it within a month, rather than 6 months after the year end allows them to understand and make adjustments in a timely manner.

Understanding the drivers of future profitability and in particular tracking the sales drivers, (transactions x average transaction value), helps maintain focus on the things that matter.

Tracking and working to move their Sales and Customer Drivers in the right direction is only possible if they are able to measure them, which is exactly what the Business Overview Report does and as the saying goes, you can only manage what you can measure.

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" You only have to do a few things right in your life so long as you don't do too many things wrong "

Warren Buffett

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1. Overview

The Business Overview Report provides the critical information about a business you need to monitor and importantly it gives an insight into not only the recent history, but also the key drivers that will impact future growth.

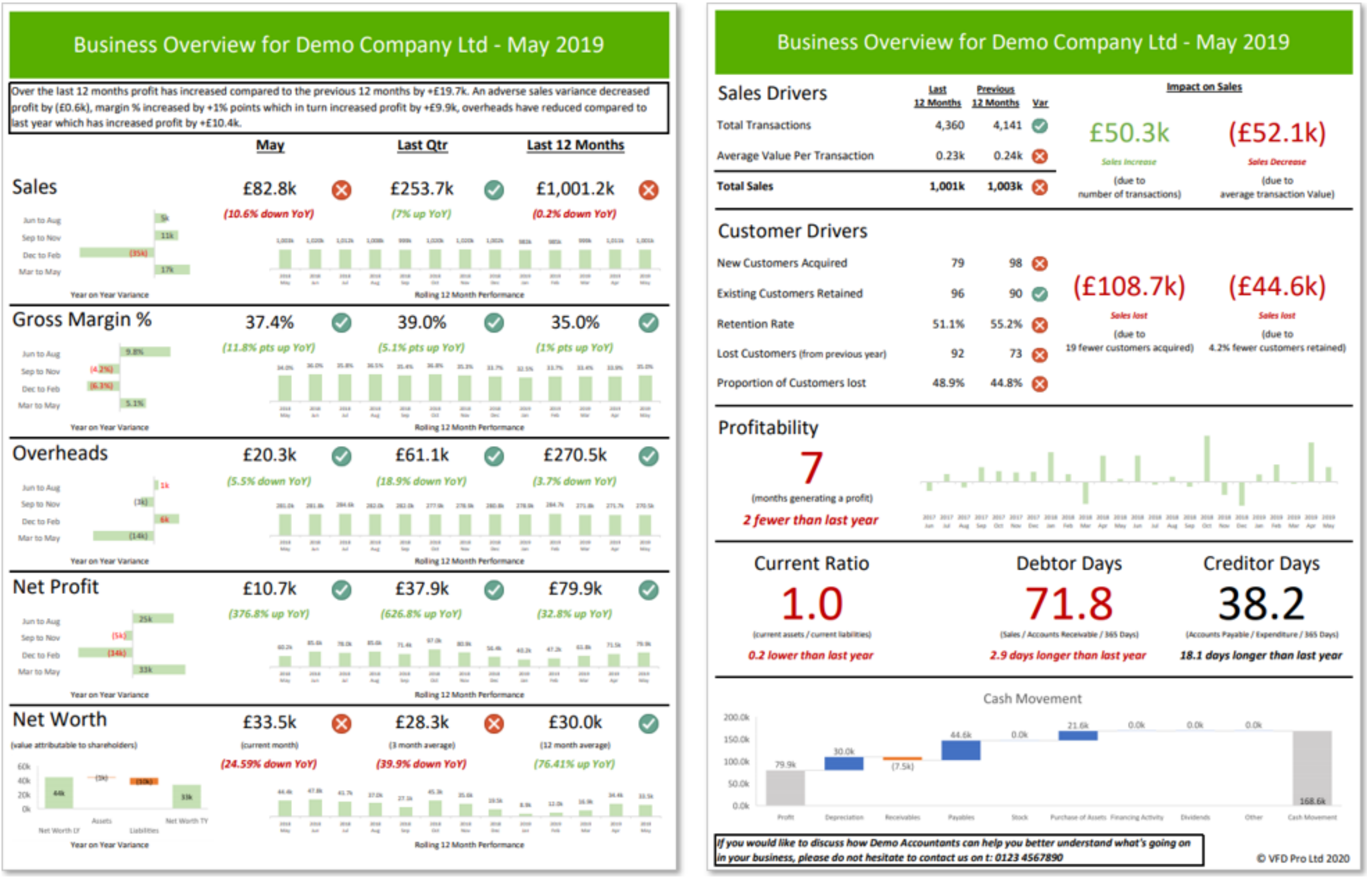

Figure 1 - Overview

1.1. Recent History:

The Business Overview Report provides a comprehensive overview of the key business data, including the last month, quarter and year and compares this with the corresponding performance in the preceding year, (providing the accounting data includes the last two years trading).

As well as the snapshot total the report also provides an overview of the last twelve months rolling average, plus the quarter on quarter variance for this year vs last for each of the following:

- Sales
- Gross Margin %
- Overheads
- Net Profit

Finally, the Business Overview Report digs into the Balance Sheet to provide a snap shot of Net Worth movement.

As Net Worth is a snap shot at a point in time, the Business Overview Report displays the Net Worth of the busines for the month of the report, the average over the last 3 months and the average over the last 12 months.

They are then compared to the corresponding period in the previous year and a waterfall chart shows the movement in net worth, i.e. the year on year variance showing how the Assets and Liabilities have moved from last year to this.

1.2. Key Sales Drivers:

Total revenue / sales is a function of the total number of transactions multiplied by the average value per transaction. Whilst most financial reports fail to identify this business-critical information the Business Overview Report provides a concise summary.

Total Transactions: The total transactions in the last 12 months is quantified and compared to the corresponding total for the preceding 12 months. If the year on year variance is positive, this is highlighted by a green tick, if it is negative, it is highlighted by a red cross along with the sales impact, positive or negative.

The impact on sales due to the movement in the total number of transactions is also shown, in green if the year on year variance is positive, and in red if the year on year variance is negative.

Average Value per Transaction: The average transaction value in the last 12 months is quantified and compared to the corresponding average value in the preceding 12 months. As with Total Transactions, if the year on year variance is positive, this is highlighted by a green tick, if it is negative, it is highlighted by a red cross.

The impact on sales due to the movement in the average transaction value is also shown, in green if the year on year variance is positive, and in red if the year on year variance is negative.

1.3. Key Customer Drivers:

Without customers there is no business, so understanding what is happening with new customer acquisition and customer retention / attrition is not just sensible, it is critical to success. It enables you to identify the underlying trends in client numbers and hence what sales might look like in the future.

The Business Overview Report identifies the total and related percentages for the last 12 months versus the preceding 12 months for each of the following:

- New Customers Acquired
- Existing Customers Retained
- Retention Rate
- Lost Customers (from the preceding year)
- Proportion of Customers Lost (from the preceding year)

The Business Overview Report also highlights the impact on the business, (positive in green, negative in red), of the difference in acquisition and retention performance in the last 12 months compared to the preceding 12 months.

Customer Acquisition: The impact of increased customer acquisition, (or reduction in customers acquired), are reported to highlight the total impact on sales, an increase in the number of new customers acquired year on year is shown in green, whereas a reduction in the number of customers acquired is shown in red.

Customer Retention: The impact of improved customer retention, (or decrease due to deteriorating customer attrition), is reported to highlight the total impact on sales, an increase in the number of customers retained year on year is shown in green, whereas a reduction in the number of customers retained is shown in red.

1.4. Profitable Months, vs Loss Making Months:

In an ideal world a business would be profitable in every month, but so long as you are making progress and making profit in more months than last year you know you are moving in the right direction, or not!

The Business Overview Report provides a 'this year versus last year' overview of profitably vs loss making months to help you keep tabs on progress and profitability.

1.5. Current Ratio, Debtor Days and Creditor Days

The Business Overview Report also analyses three additional items of business critical information:

- Current Ratio
- Debtor Days
- Creditor Days

The current ratio is a measure of a business' ability to pay liabilities. A current ratio of one or better is good, whereas a current ratio of less than one is not desirable so a negative trend, (highlighted in red), is cause for concern, which leads us to Debtor Days and Creditor Days.

Many businesses focus on making sales and delivering the goods or services they sell and as a consequence don't focus on collecting the money they are owed. If debtor days are high, your clients are acting as their customer's bank giving extended credit, and a negative trend, highlighted in Red, indicates the situation is getting worse. The faster businesses get cash from their customer's bank account into their own the better.

Creditor days are a bit different, in an ideal world a business will agree extended credit terms with their suppliers, after all, the longer they can keep their cash in their bank the better.

1.6. Cash Movement

Many business owners lament the fact that their accounts tell them they are profitable, but their bank balance appears to tell another story. The waterfall chart provides an overview detailing the elements that make up the difference between profitability and cash movement.

2. Page 1: Performance over the past 12 months

This one page provides a good understanding of performance over the past 12 months with a comparison to the preceding 12 months for sales, margin, overheads and net profit plus the movement in net worth. Let's look at each part of the report…

2.1. Movement in Profit in Words

Profit performance in the last 12 months is summarised in words to detail the movement in profit this year compared to last year and where that profit movement came from, in other words how much of the total movement came from sales, gross margin and overheads.

> Over the last 12 months profit has increased compared to the previous 12 months by +£19.7k. An adverse sales variance decreased profit by (£0.6k), margin % increased by +1% points which in turn increased profit by +£9.9k, overheads have reduced compared to last year which has increased profit by +£10.4k.

Figure 2 - Profitability in Words

2.2. Sales Overview

Sales performance over the last 24 months is used to provide the overview. Starting with the most recent month compared to the corresponding month from last year, the most recent quarter, and the last 12 months.

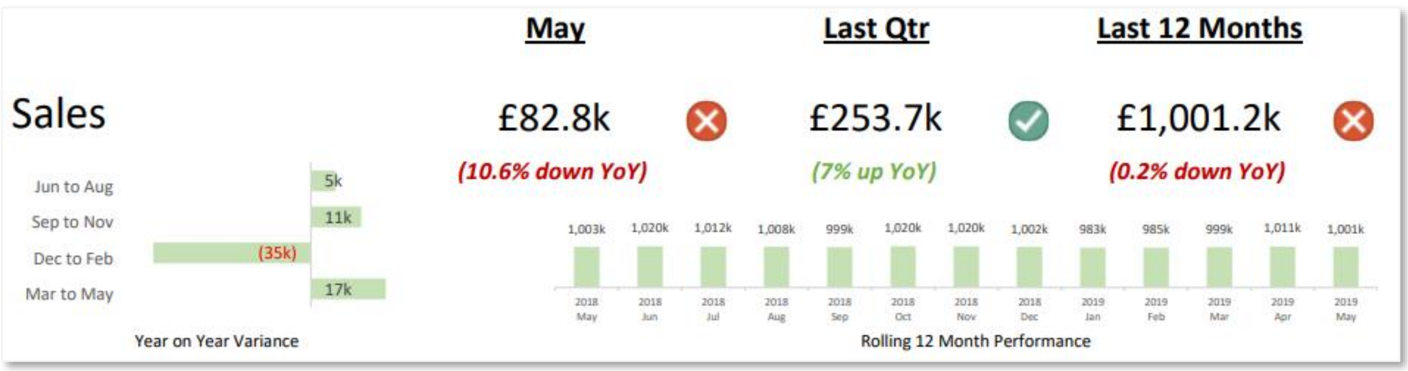

Figure 3 - Sales Overview

A positive variance is highlighted with a green cross, whereas a negative variance is highlighted with a red cross. The percentage improvement (highlighted in green), or deterioration (highlighted in red), is also shown providing a quick and easy way to track overall sales performance.

Then we look to understand the quarterly variation, in the illustration above the greatest variation is in the Dec to Feb period where turnover was down by a total of £35K, this is more or less offset by the gains in the other three quarters.

The rolling 12 months average sales are detailed in the column chart, which in the demonstration company illustrated above shows a very stable sales performance, but unfortunately, in this example sales year on year are very slightly down, so this company is more or less 'flat lining' on sales.

In summary, for the demonstration company illustrated above, we can see that sales are not growing, which means any improvement or deterioration in profitability is not due to a movement in sales. Whilst there is no growth, it is not a disaster either, to understand the full picture we need to know what else his happening in the business.

Note: *If less than 2 years data is unavailable the this year vs last year comparison cannot be shown, but as soon as there is 24 months history, all of the detail described above will be included, until then only a sub set of the above information will be included.*

2.3. Gross Margin % Overview

Gross margin % is reported in the same way as sales, comparing the most recent month, quarter and year with the preceding period and highlighting a positive or negative variance with the green tick or red cross and the percentage movement year on year.

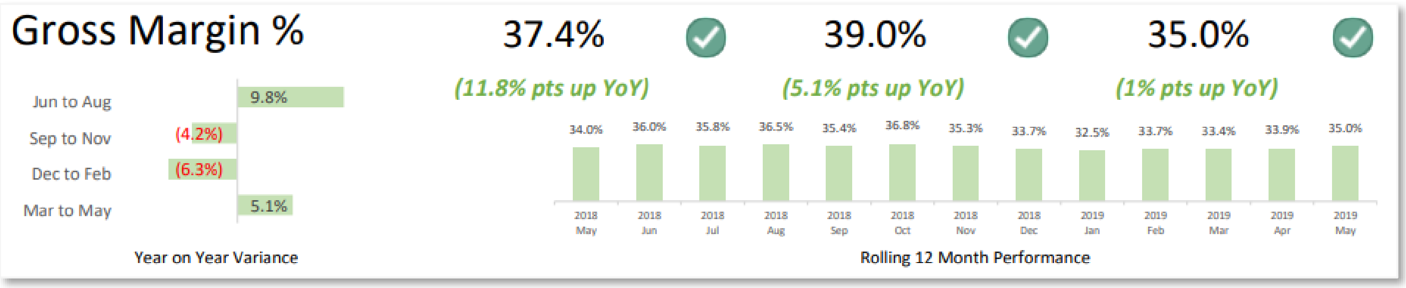

Figure 4 - Gross Margin %

For the demo company example used above you can see there is a marked improvement in profitability for the month, quarter and year to date. The last month and quarter in particular show a very significant improvement with the most recent month showing nearly a 12% improvement in gross margin %.

One might assume the business owner in this case is comfortable with the margin rate improvement, maybe it could be better, but we would need more analysis to address that, in the meantime, let's look at the third driver of profit, overheads.

2.4. Overheads Overview

Your overheads are reported in the same way as sales and gross margin %, comparing your most recent month, quarter and year with the preceding period and highlighting a positive or negative variance with a green tick or red cross and the percentage movement year on year.

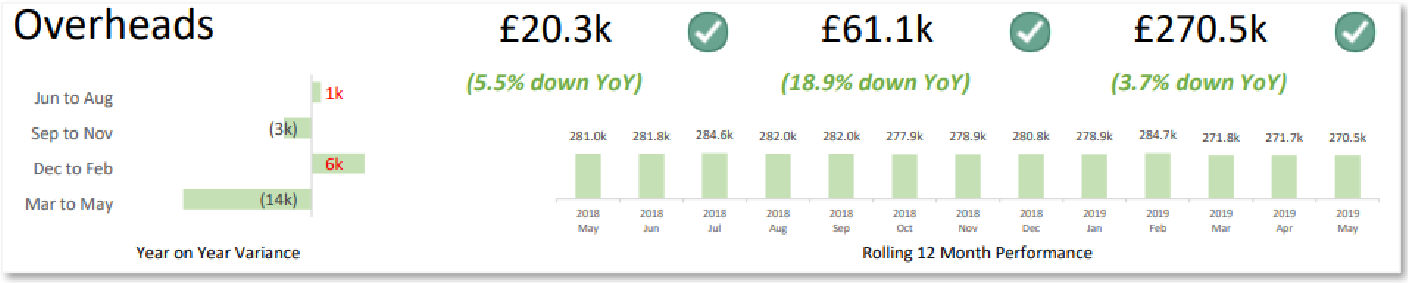

Figure 5 - Overheads

In the case of the demo company, we can see that overheads are another success story with total overheads this year down 3.7% on the previous year. So, whilst sales are flat, this company has seen a significant improvement in gross margin % and a reduction in overheads so one would expect the net profit to have increased…

2.5. Net Profit Overview

Net Profit is reported in £ rather than % and as expected, the demo company has seen a substantial increase in profitability. This is reported in exactly the same way as sales, gross margin % and overheads, and in this case you can see that profit this year is up 32.8% on last year and everything is showing as green, indicating a positive year on year variance.

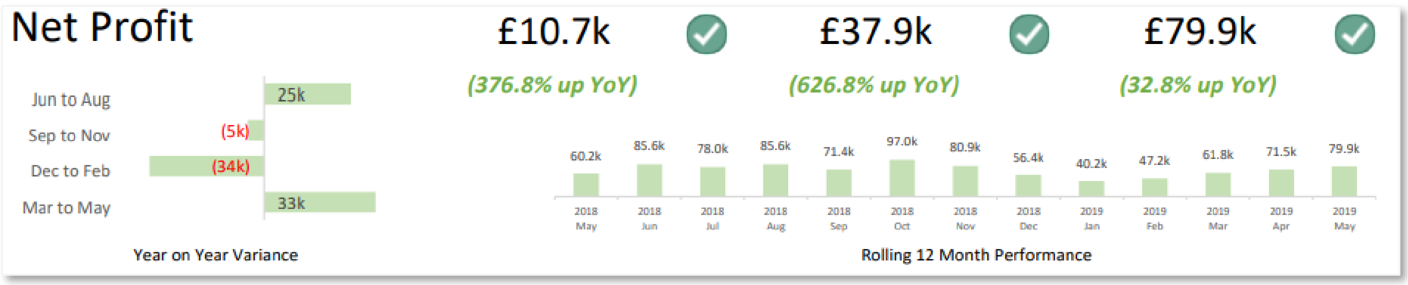

Figure 6 - Net Profit

With improvements in profitability one could speculate that the business owner in this case is very pleased with the direction of the business and with a 32.8% increase in year on year profits, is highly likely to be paying themselves a significantly larger dividend than last year.

One would assume the net asset value of the business has increased considerably, but it looks like more investigation is needed because the last part of the report on page one, takes a quick look at this.

2.6. Net Worth Movement

The last item on the report is Net Worth, and whilst this is slightly different to all the other figures reported because it is a 'snap shot' of the balance sheet, it is showing that the net worth of the business has deteriorated.

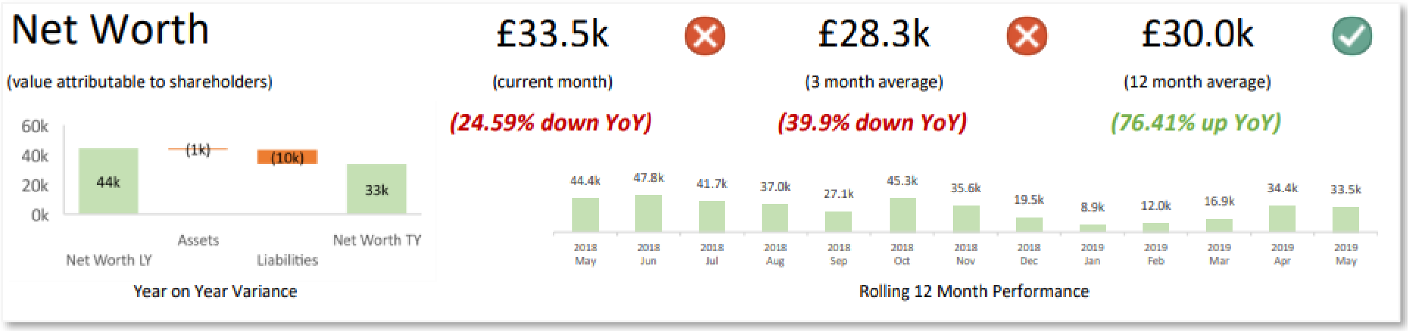

Figure 7 - Net Worth

Net worth on the balance sheet this time last year was £44K, whereas this has reduced to £33K this year driven by a minus £1K movement in the company's assets and a £10K increase in liabilities.

This may not be a problem, but we would need more information than is presented in the Business Overview Report to be able to understand and explain exactly what is going on.

Everything we have discussed so far provides a good overview of the most up to date history, clearly we could go into much more detail on what has happened, for now, let's move onto look at the critical LEAD indicators for every business and go through page 2.

3. Page 2: Key Performance Indicators

Whereas sales, gross margin %, overheads, net profit and net worth are all very important, they all have one thing in common, they are what is known as 'Lag Indicators', in other words they have already happened so whilst we are reporting on the very recent past, it is still history.

It would be fantastic if we could predict the future and if we could we would no doubt be doing something else entirely, but in business the next best thing is 'Lead Indicators', these are the Key Performance Indicators that tell you what is going to happen in the future.

For most companies sales are critical and as the saying goes, nothing happens in business until a sale is made and in most cases sales come as a result of having customers so it makes sense to understand what the key trends in a business' customer base are, which is where Page 2 of the Business Overview Report goes next.

3.1. Your Key Sales Drivers

Sales are made up of two things: The number of transactions and the average transaction value, so if you know the total number of transactions and the average sales value, one times the other = sales / revenue.

Total Transactions: The Business Overview Report starts by highlighting the total number of transactions the business made (defined as a line within an invoice) with customers in the last 12 months and compares this with the corresponding period in the preceding 12 months.

An increase in the number of sales transactions is highlighted with a green tick, whereas a negative variance is highlighted by a red cross. The Business Overview Report then provides an indication of the impact the movement in the number of transactions has on total sales.

Sales Drivers	Last 12 Months	Previous 12 Months	Var
Total Transactions	4,360	4,141	✓
Average Value Per Transaction	0.23k	0.24k	✗
Total Sales	**1,001k**	**1,003k**	✗

Impact on Sales

£50.3k	(£52.1k)
Sales Increase	*Sales Decrease*
(due to number of transactions)	(due to average transaction Value)

Figure 8 - Sales Drivers

Using the average transaction value, the difference in total number of transactions, positive or (negative), can be used to establish the corresponding impact on total sales which in the case of the demo company is a success story. The increase in the total number of transactions should have contributed an additional £50,300 to total sales, however, to get the full picture we also need to understand what happened to average transaction values.

Average Transaction Value: In an ideal world you would focus on improving both of these important KPIs. The Business Overview Report helps achieve this by highlighting the underlying trend and reporting on the Average Value per Transaction in the last 12 months compared to the previous 12 months.

There could be many reasons for a reduction and whilst these may be outside the control of the business in far too many cases the causes are totally within the control of the business, with discounting being a frequent culprit.

As with the total number of transactions an improvement is highlighted by a green tick, and as can be seen in the above example, a negative movement is highlighted with the red cross. The Business Overview Report will then seek to quantify the sales impact of the movement, which in the above example indicates that this has written off all the gains made by increasing the total number of transactions resulting in the deterioration in sales year on year.

We now know what has happened to sales and can better explain why this business has moved from £1,003K to £1,001K, but what is likely to happen in the future?

3.2. Your Key Customer Drivers

Transactions are a function of customer numbers and all things being equal, the best way to increase the number of transactions is to increase the number of customers. This thought process leads us to consider what impacts the number of customers, which is exactly what the Business Overview Report identifies next.

In the future, the total number of customers will be a function of two things:

- The rate and hence number of new customers acquired
  and
- The rate and hence number of existing customers lost

A business can be considered to be like a leaky bucket, every business will lose customers from time to time, that is inevitable, but if they loose customers faster than they acquire new customers the bucket (the number of customers serviced), will inevitably start to empty.

Figure 9 - The Leaky Bucket: Customers In & Customer Out

New Customers Acquired: There are clearly a lot of factors that will influence a business' success in attracting new customers and whilst these may not be totally within their control, one thing is certain, if you don't measure you cannot manage.

The Business Overview Report identifies the number of new customer acquired in the most recent 12 months and compares this to the corresponding period 12 months prior to highlight a positive or a negative variance, (with the green tick or red cross respectively).

Customer Drivers	Last 12 Months	Previous 12 Months	Var
New Customers Acquired	79	98	✗

Impact on Sales

(£108.7k)

Sales lost

(due to
19 fewer customers acquired)

Figure 10 - Customer Drivers – New Customer Acquisition

To help you understand the potential financial impact, the Business Overview Report will also highlight the potential commercial impact of any change in customer acquisition year on year.

In the example above, in the last 12 months the business acquired 19 fewer customers and all things being equal, the impact this has had on sales is a decrease of £108.7K, which represents more than 10% of total sales, so for the demo company this is clearly a big issue and one that needs focus and attention.

Let us now look at the corresponding Lead Indicator, the rate of client retention, (or attrition).

Customer Drivers	Last 12 Months	Previous 12 Months	Var
New Customers Acquired	79	98	✗
Existing Customers Retained	96	90	✓
Retention Rate	51.1%	55.2%	✗
Lost Customers (from previous year)	92	73	✗
Proportion of Customers lost	48.9%	44.8%	✗

Impact on Sales

(£108.7k)

Sales lost

(due to
19 fewer customers acquired)

(£44.6k)

Sales lost

(due to
4.2% fewer customers retained)

Figure 11 - Customer Drivers - Customers Retention

Customer Retention is perhaps THE most important area for focus, but tragically it is seldom if ever a part of the financial reporting pack which is why the Business Overview Report analyses and provides so much invaluable management information to help the business owner understand and better manage the key drivers.

The following are included in the report comparing the last 12 months to the previous 12 months:

- The number of existing customers retained
- The retention rate as a percentage of last year's total customers
- The number of customers lost (from the previous year)
- The proportion of last year's customers lost as a percentage of total customers

Every business is different but the key factor to focus on is the rate of customer retention, (or its inverse, the rate of customer attrition).

For the demo company illustrated above the underlying trend is moving in the wrong direction, the indication is that retention is getting worse year on year by 4.2%, so all other things being equal, unless something changes, it is reasonable to assume this deterioration will continue into the future.

The impact of the deterioration is again highlighted in terms of its potential impact on sales, i.e. 4.2% customers has potentially reduced sales by a further £44.6K.

If we then look at the total potential lost sales as a result of a deteriorating rate of customer acquisition, retention and in this case the erosion of the average value per transaction this comes to £205.4K, which for a company with revenue of just over £1M represents 20% of turnover.

Another useful way to reflect on the full impact of this negative trend is in terms of lost profit potential. We know this company is trading with a 35% gross margin, so had the company simply maintained last year's performance with regards average transaction value, acquisition and retention, profits could have increased by nearly £72K.

3.3. Profitable vs Loss Making Months

In an ideal world every month would be profitable however many businesses experience seasonality in their trading with a mix of profitable and loss-making months. It is sensible to keep track of the underlying trend which is where the next part of the Business Overview Report goes, by highlighting the number of months in which a profit was generated and comparing this to the previous year.

If the company has made profit in fewer months this year than last this is highlighted in red as shown below where this particular company made profit in 7 of the last 12 months, whereas in the preceding year, they made profit in 9 months, a deterioration of 2.

Figure 12 - Profitable Months This Year vs Last Year

The column chart shows the variance positive or negative above and below the datum line and the size of the bars represents the total profit, (or loss), made in each of the last 24 months.

3.4. Current Ratio, Debtor Days and Creditor Days

The current ratio is an indication of a company's liquidity and it should be noted that current ratios tend to vary from industry to industry.

A high current ratio is generally better than a low current ratio, because it indicates that the company is more capable of paying its creditors. If the current liabilities exceed current assets the current ratio will be less than 1.

A current ratio of less than 1 indicates that the company may have problems meeting its short-term obligations.

Current Ratio	Debtor Days	Creditor Days
1.0	71.8	38.2
(current assets / current liabilities)	(Sales / Accounts Receivable / 365 Days)	(Accounts Payable / Expenditure / 365 Days)
0.2 lower than last year	***2.9 days longer than last year***	***18.1 days longer than last year***

Figure 13 - Current Ratio, Debtor Days and Creditor Days

Whilst a more in-depth analysis and evaluation of options would be advisable, as you can see, the Current Ratio for this business has moved from a positive 1.2 last year to 1.0 at the time of this report.

Once again, if this trend continues and no action is taken, this could well indicate an impending cash flow crisis so the sooner the business can take positive steps to reverse the trend and/or increase liquidity the better the chances of a successful outcome.

As the saying goes, 'Turnover is Vanity, Profit is Sanity, but Cash is Reality', anything a company can do to improve their cash position should be a focus which is where the Business Overview Report goes next, by looking at Debtor Days and Creditor Days.

Debtor Days: The most obvious way to get more cash into a business is to collect cash from debtors. Think of it this way, it is the business' cash, they are bankrolling their customers and they don't even earn interest on the loan. So how long are their customers keeping hold of their money before paying them for the goods and services they have provided.

Debtor Days is the number of days, on average, a customer takes to pay. In general, the lower the debtor days the better and a well-run business will always aim to keep debtor days to a minimum. Whist average Debtor Days vary from industry to industry, taking 71.8 days to collect the money owed to a business, on face value, does not look like a well-run company, but how about the underlying trend?

As you will see in this example the situation is getting worse and the fact that it has increased by 2.9 Days since this time last year indicates yet another potentially worrying trend, what might this be next year.

Creditor Days: Creditor Days is not colour coded because increasing the time taken to pay suppliers can be considered a good thing as it keeps cash in the business. However an average increase in creditor days by 18.1 days to 38 may imply problems paying suppliers and one could speculate that suppliers are being stretched excessively which may lead to poorer credit terms (or a success story if the increased terms were negotiated).

The Report then seeks to clarify how the profitability and cash movement relate to each other.

3.5. Profitability vs Cash Movement

Many business owners wonder why their accounts say they are making a profit and yet there is no cash in the bank, (or possibly the other way round).

The movement of cash in a busines can be complex but the waterfall chart at the bottom of page 2 seeks to clarify this by identifying the Profit generated and then showing the impact of movements in the following:

- Depreciation
- Receivables
- Payables
- Stock
- Purchase of Assets
- Financing Activity
- Dividends
- Other

The report concludes by highlighting the Cash Movement in the business over the last 12 months.

4. List of Figures