Successful Financial Management

What is Financial Management and why is it so important? What does it mean to be successful in Financial Management?

Many business owners and employees in other departments wonder about the “bean counters” - those who enjoy working with numbers, processing financial transactions, and analyzing financial statements. Bookkeepers, clerks, accountants, controllers, and even CFOs may be considered just a little “unusual”, but smart business owners value them for what they do and for how they contribute to the health of the company.

Businesses do not survive very long without the ability to successfully manage their finances. All strong businesses process financial transactions effectively and efficiently, create great financial plans, monitor progress against those plans, and make adjustments to company behavior when financial reality doesn’t match up with the plans. You have to be good at the books to be good at business.

We say that the functions of Financial Management include these eight areas:

- Creating a Profitable and Sustainable Financial Model,
- Bookkeeping and Accounting Controls,
- Running Your Company “By the Numbers”,
- Managing Your Cash,
- Risk Management,
- Asset Management,
- Understanding and Managing Your Funding Options, and
- Understanding and Managing Your Value Drivers.

Creating a Profitable and Sustainable Financial Model

It is no simple task to create a workable financial model for a business in which you have little financial experience. Even those who are great at creating products and / or delivering services may not understand how to translate that talent into a profitable business. Owners need to charge a fair price and hold operating expenses to reasonable levels. They have to make reasonable financial projections, forecasts, and budgets, and understand what a solid business in their industry looks like. Creating that model is the first function of Financial Management.

Business owners and senior executives should understand both the language and the concepts of accounting, especially revenues, gross margins, operating expenses, operating incomes, EBITDA

(Earnings Before Interest, Taxes, Depreciation, and Amortization), pre-tax income, and cash flow. They should understand what is represented on the Profit & Loss (Income) Statements, Cash Flow Statements, and Balance Sheets and use them to manage the business.

Bookkeeping and Accounting Controls

It is important to process and post your financial transactions promptly and with careful attention to detail. There are several common-sense reasons for doing so. For example, you may save money by taking early payment discounts and by avoiding late fees and / or overdraft penalties. You can also accelerate revenue and improve cash flow by processing invoices promptly and sending timely statements. When you pay bills on time, you protect your credit record, thereby increasing your ability to negotiate special terms and prices and keeping your funding options open. It is also important to be accurate so that you will be able to properly analyze your financial performance.

Management is also responsible to do everything within its power to ensure the company's financial security, and one key to that is to put controls in place that prevent fraud or embezzlement. The systems used by many small businesses lack appropriate audit trails, so management must be aware of their exposure and use additional procedures to ensure that checks and balances are in place. You have a responsibility to your employees to both remove temptation and to protect them from suspicion, and to your investors and other stakeholders to ensure that their financial position is secure. Controls and procedures should be in place to discourage and prevent fraud, and the financial results should be periodically reviewed or audited by an independent third party.

Running Your Company "by the Numbers"

Managers should regularly create expense budgets and revenue forecasts, and review company progress against those plans. There should be no doubt about the current financial position, planned income and expenses, and funding requirements.

Your budget is your financial plan. It is a good practice to develop your budgets on an annual basis, and then to compare them with your actual results each month. You are certain to have variations between your budgets and your "actuals", and you should analyze those variations to determine if they are random, significant, the result of a posting error, or the result of an unauthorized expenditure. Whenever you find a variation, you should also look at your year-to-date results to see if the difference is made less significant by counter-balancing variations in other months, or if there is a trend that requires some action.

Managing Your Cash

"Cash is King" is one of the cornerstone sayings of business, and it is important to do everything in your power to ensure that your enterprise has good cash flow. Cash is the lifeblood of your business. Your business runs much smoother if you do not have to keep a nervous eye on your bank balance.

The negative consequences of a cash flow crunch can be quite severe: you may not be able to get the supplies you need to serve your customers, you may have to borrow money at excessive interest rates, you may cause legal issues by missing tax payments, and you may even not have enough cash for your payroll. Relationships will suffer both inside and outside the company, especially if you miss a payroll. The business owner usually suffers above all others, as it is their compensation that gets cut first, and most.

The bottom line: when you run out of cash, you may be run out of business. Get the funding you need, before you need it, to avoid that problem.

Risk Management

Risk Management requires having appropriate insurance policies in place to mitigate losses that happen from accidents, mistakes, and other aspects of “everyday life”. Those policies may include (but are not limited to) to the following:

- Property and Casualty Insurance,
- Automobile and Truck Insurance,
- Key Man Insurance,
- General Liability Insurance,
- Errors and Omissions Insurance,
- Professional Liability Insurance,
- Directors and Officers Insurance, and
- Workers’ Compensation Insurance.

Asset Management

Asset Management means you have the appropriate security in place (physical and electronic / Internet) and that you are tracking company assets appropriately. For most companies, that means having simple systems in place to track all of the assets (furniture, equipment, software, vehicles, inventory, etc.) whether on the books as an “asset” or not. Those records should also include the initial asset value, the chosen depreciation method, and the amount that has been depreciated to date.

Asset management also means protecting your intellectual property via the appropriate trademarks, copyrights, and patents. It means having an intellectual property attorney routinely look at the many trademarks and patents that are “published for opposition” and respond accordingly when someone violates your intellectual property rights.

Understanding and Managing Your Funding Options

Creating financial strategies requires knowledge of your available funding options and managing those carefully. Funding options include debt, equity, and supply-chain financing, and each comes in many different flavors. For example, debt financing can be in the form of conventional business loans, home-equity loans or lines of credit, SBA loans, signature loans, and receivables factoring, among many others. Understanding the capitalization process and the regulations that apply to sharing a secured interest in your company will present opportunities not available through other funding options.

Understanding and Managing Your Value Drivers

Company management should understand how the company is valued and what their value drivers are so they can adjust strategic plans to maximize the asset value of the business, and it is important that management review the asset value of the company on a regular basis. That value is based on value drivers, such as the Owners Discretionary Cash Flow, the number of customers, the asset value of plant and equipment, and the reputation (goodwill) enjoyed in the marketplace. The way to determine a company's value drivers is talk to business brokers and other financial advisors who can tell you how investors and potential purchasers of the business may value it. Once you know how others may value your business, you can put plans in place to increase the value of your business by focusing on the growth of the value drivers.

How are you performing in Financial Management? Do you need training or coaching? Do you have reliable controls in place? Do you have the funds you need to safely operate your business?

If we can help you be successful in Financial Management, or any other aspect of your business growth, please give us a call or email!

Paul Hoyt

Hoyt Management Group

www.PaulHoyt.com
415.997.8001
paul@paulhoyt.com