FINANCE FOR NON-FINANCIAL MANAGERS

Don't be put off by financial jargon. Shaz Nawaz explains why learning about company finance is so important when measuring success.

Finance is at the heart of every successful company, it's the story behind the scenes. It shows you the correlations and the implications of management decisions and helps direct what you should and shouldn't do. You certainly don't need to be a maths genius to make sense of your figures. All you need is a basic understanding of what the numbers mean. There are a number of different ways to measure a company's financial performance. Here are a selection of terms and what they mean.

Profit and Loss (P&L) account

Profit and Loss account - a statement which shows you how your company has performed, usually over a 12 month period (although it can be for a shorter period.)

Turnover - shows you how much income you have generated.

Cost of Sales - the expenses which relate to making a sale.

Gross margin – this is the important one! You can work out your Gross Margin by dividing your Gross Profit by Sales. The number you're left with should remain consistent and even grow over time. Remember 'Gross' is different to 'Net'. 'Net' is normally used after taxes and all costs have been removed from the 'Gross' figure.

Net Profit - derived by deducting all of your expenses, including tax (such as VAT), from your income. It is important to note that your Bank Balance and Net Profit are two different numbers. The Cash Balance is how much money you have in the bank. It does not take into account how much money is owed to you or how much money you owe.

Balance sheet

This is the statement which tells you if your business is trading as a 'going concern'. In simple terms it is divided into assets and liabilities. Your assets have to be greater than your liabilities in order for you to be solvent and therefore a going concern.

Management information

This is data which is particularly important to you when it comes to making business decisions. It helps you to make sound decisions while giving you an understanding of your current position. Your accounts do not track numbers like sales conversion rates, debtor days, customer feedback, employee satisfaction and so on. This, therefore, means it is vital that you have a management information process where you track key numbers outside the scope of standard accounts. As you track your key numbers and review your position, you may start to think differently and see the power of being able to read accounts effectively.

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Jargon buster! Common finance terms

There are three main financial statements, **Profit and Loss** (P&L), **Cash Flow Statement**, and **Balance Sheet**.

The **P&L account** shows whether, over a period of time, a business made a profit or lost money.

The **Cash Flow Statement** shows how money flows into and out of the business over a period of time.

The **Balance Sheet** gives a snapshot of the business at a fixed point in time.

Working Capital is the money needed to fund the business's operation.

Costing and Pricing aims to find the price the business should charge bearing in mind the market place in which it is operating.

The **Break-Even Point** is useful when it comes to setting sales targets. This is the point at which the company's costs are met to continue to operate.

When cash is king

Ted Wainman, professional trainer and author explains how to apply financial theory to solve real life business problems.

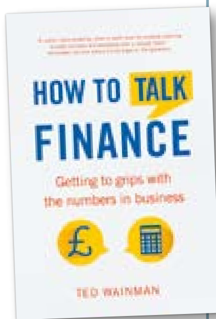
Real life business problems usually stem from inadequate cash flow (sometimes referred to as 'liquidity'). Liquidity is defined as 'the ability of the company to meet its obligations as they fall due' – so just as you will focus on ensuring that you have sufficient cash to pay your bills (using credit cards and overdraft facilities to manage short term cash flow issues) so a company must ensure that it remains liquid.

The income in your budget, however, is not shown when the cash is received and the costs are not shown when the cash is paid out – rather income is recognised when the goods are sold or the service delivered. Likewise, the costs are reflected in the budget when the goods are delivered or the service received.

So what can you do to help with a company's liquidity? When negotiating sales contracts, remember that it is not just about selling as much as possible for as high price as possible, but also about ensuring that the terms of sale allow for early collection of the amounts due – payment terms of 30 days are preferable to 60 or even 90. There is less chance that your customers will be unable to pay and you will receive the cash earlier. When negotiating supplier contracts, a low price is desirable, but so are later payment term.

If you operate in a company with stock, the final focus for improving liquidity is stock turnover – in effect the speed at which you can convert a purchase of a good into a sale. If you sell lettuces, this should be fairly quick; aircraft carriers may take a little longer.

Budget holders will often be measured on the ability to shift stock, pay suppliers later or collect monies due from customers quickly, as well as their ability to increase sales or reduce costs. Cash is king, as the mantra proclaims. So when managing your budget for your business unit, consider the extent to which you are generating cash for the business or the extent to which you create a cash strain on the business.



Manager has a copy of Ted Wainman's book "How to Talk Finance: Getting to grips with the numbers in business" to giveaway. To be entered into the draw to win, email manager@instam.org with the message "Help me talk finance!" by September 30th. First name chosen at random will receive the book!

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