Be more profitable with creative accounting

Three plans for using your monthly profit-and-loss statements to bump your bottom line.

by Dan Saunier

■ Accounting statements, by their very nature, are based on historical information. What will happen in the future, however, is up to you. And you can use this month's information to help increase your profits next month.

First and foremost, you need to change the way you think while reading your income statement. Use it for laying out the same time period in the future. Ask yourself the following "will" questions:

1) Will my sales be the same for the next period?

2) Will my gross profit be the same next month?

3) Will labor costs remain the same next period?

4) Will my supplies/inventory balances increase or decrease?

5) Will my cash balance change next period?

6) Will my new income change next period?

Now, based on the answers, you can move to the next set of "how" questions:

1) How can I increase sales?

2) How can I reduce labor as a percentage of sales?

3) How can I increase my gross profit margins?

4) How will sales affect my supplies/inventory balances?

5) How can I increase my cash balances?

6) How can I increase net income?

After answering these questions, you have the basis for a financial plan. But be sure to test each aspect of the plan against the current financial information.

Assuming that you can increase sales, what numbers from the most recent period will change? Labor costs may or may not change. Fixed costs are unlikely to change, but part of the increased sales revenue may be coming from additional advertising or promotional expenses. Net income under this new model will probably change, and will this be for the better?

By using the income statement from the prior period, you can develop your future plans. Just make sure that your plans are simple, with only a few objectives each period, so as to not overwhelm yourself and diffuse your focus.

What if???—A second approach is to use the "what if" question on your financial information—a variation on the "will and how" idea. In this approach, you need to review each line of your income statement with the following question in mind: What if I increase or decrease this revenue/-expense line by 10 percent?"

For example, "What if I increased my advertising expense 10 percent? Would my revenues more than compensate for the additional expense?"

Or, "What if I reduced my advertising expense 10 percent? Would my revenues decline beyond my savings in expense?"

Once you have examined each line in this manner, look beyond the next financial period. Sometimes short-term gains result in long-term losses. We often look at ways to decrease expenses instead of looking at "good" investments that may temporarily increase expenses but will result in long-term net income gains. Look in both directions.

Remember: only you, as owner, can answer the "what if" questions. Net income is on a curve, not a pillar. A small change will not cause your net income to go to zero, but rather to another position on the curve—perhaps a better position. Experiment to find the range of possible outcomes.

Keeping score—Finally, you can use the income statement as a scorekeeper, to keep track of your progress toward defined goals.

At the beginning of the year, set up three major financial goals for your company. The goals should be exact, and mathematically expressed. Your reach should exceed your grasp. For instance: increasing sales by 19.5 percent, reducing labor to 4.5

percent of sales, increasing average cash balance to $10,500, etc.

At the end of every financial period, review where you are. Set up a chart in your office. Pin notes on your desk. Make the representations as visual as possible. Then, each month, adjust your progress based on your financial reports.

Financial reports, on the whole, tell you where you've been. But you spend too much time, energy and money on them not to squeeze every last benefit out of them.

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