

## WHAT DO THOSE FINANCIAL STATEMENTS MEAN?

Financial Statements - UGGHH!!! Confusing, unnecessary, complicated, and irrelevant - just some of the words often used to describe these much underestimated and under-utilised sources of business information.

There is no doubt that in their purest form they can be austere and complex - but for management purposes they need not be so.

In fact as owners and managers making decisions affecting the business daily, you should be sufficiently familiar with what your financial statements mean, and how to use them, to be able to put together a simple, information picture of your business at any point in time to assist you with decision-making.

### WHY NOT JUST LEAVE IT TO THE ACCOUNTANT?

Obviously your accountant has an important role to play, particularly in providing management information on an annual basis.

But in order to maximise your business returns, it's important for you to develop your skills in this key area of understanding and using business information.

### WHICH STATEMENTS ARE IMPORTANT?

Basically there are three aspects of business performance which need to be measured, so there are three different statements which reflect those measures. Generally, accountants will provide you with the first two each year.

**The Profit and Loss Statement** measures profitability. It is like a history book of the business and shows for a past period of time how much has been generated in the way of revenues and expenses. The difference between these two items is the net profit or loss for the firm.

**The Balance Sheet** on the other hand measures the value of the business. It is like a photograph of the business at a particular point in time and shows the value of what you own (assets), what you owe (liabilities), and the value of the owners investment in the business (owners equity). Owner's equity is simply the difference between what the business owns and what the business owes.

**The Cash flow Statement** measures liquidity. It is like a crystal ball for the business in the sense that it is usually used for a future period of time to show where cash is likely to come from and where it is likely to go. (The Cash flow Statement can also be used for a past period of time to see where cash has come from and gone to.) It is a simple measure of cash in to cash out.

### WHAT ARE THE IMPORTANT THINGS ON THESE STATEMENTS?

While all the figures contained in these statements are important and useful for management purposes, there are some key figures which can be used to achieve and maintain regular control within the business.

At this stage, the most important items to keep track of are simply Profit and Cash - two figures which are often confused but are in fact completely different.

A quick comparison between the end of year cash position (shown on the bank statement) and the end of year profit position should be enough to convince most managers that there is little similarity between the two figures. However, an overwhelming number of owners and managers neglect to plan for cash, and assume the balance at the bank is their profit.

Lack of cash is possibly the single largest contributing factor to the failure of many businesses. Long-term business survival and growth rest heavily on the ability of the owner/manager to understand the difference between profit and cash, and then plan for both effectively.

### **YOUR RESPONSIBILITY AS A MANAGER**

As owner or manager you should be able to draw up a simple one of these statements at any point in time in order to monitor and assess your business performance whenever you choose.

In this way, it is no longer necessary to wait till the end of the year for the accountant to produce the information needed to make daily management decisions. Managers can produce and interpret the information themselves.

The statements don't need to be complicated. They are simply designed to reflect the operation of the business in such a way that it is easier for you to see where to direct your management attention.

You owe it to yourself and your staff for the time and effort invested in the business to have a full understanding of the way, and exactly how well, your business is operating.

Take time now to start developing your financial management skills and, chances are, you'll find you'll start to work smarter rather than harder.