12 Common Mistakes Business Owners Make

Insights from a business advisor

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Contents

Introduction....2

#1: *Profit* and *cash flow*: they're not the same thing....3

#2: Making financial decisions *without* proper analysis....4

#3: No formal business action plan in place....6

#4: Competing on price, not value....8

#5: All sales are *not* created equally....9

#6: Blaming poor performance on external factors....11

#7: Not having the right people doing the right things....12

#8: Not understanding the financial impact of operating deficiencies....14

#9: Lack of processes to manage and maximize cash flow....16

#10: Not recognizing the *Six Drivers of Profitability*....19

#11: Lack of leadership to guide and empower the team....22

#12: Not articulating the vision for your business....24

About the author....26

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Introduction

As a professional accountant and business advisor, I work with a variety of really smart, creative and highly respected business owners. However, I have also observed them missing opportunities to improve their business and help them reach the level of success they deserve. Some of these oversights stem from a lack of financial knowledge. Others come from a lack of understanding of the connection between the day-to-day activities of the business and the financial results those activities will generate. But *all* of them can have an effect on the bottom line of the business - and not in a good way!

In the pages that follow, I address the ***12 most common mistakes*** I have seen business owners (even the really smart ones!) make time and time again. The good news is that these mistakes can be corrected or avoided altogether. So, consider this a friendly heads-up from your external CFO and business advisor. My hope is that, armed with this bit of information, *you* can avoid these errors right from the start and make the best decisions possible for your business to thrive.

If after reading this report you can relate to any or many of these mistakes and would like to discuss the positive impact you can make to your business by addressing these issues, give me a call at 403.228.2535 or send me an email to steven@businessworkscas.com. I would be interested in talking with you about your business and how I can help.

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1 *Profit* and *cash flow*: they're not the same thing

Mistake #1 grows from the common misunderstanding of the difference between *profit* and *cash flow*. While this is a basic premise of accounting, many entrepreneurs don't fully grasp the concept. For example, I am regularly asked by new clients, "If I made $70k last year, why don't I have that much in my bank account?" The answer: profit doesn't equal cash flow.

Profit is the difference between revenues and all your business expenses. It appears only on the company's income statement. Your profit exists on paper, but most often will not be reflected in your bank account. Profit adds to the equity of your business and is a metric that 99 percent of people both within and outside of the business understand and readily refer to on a regular basis.

"If my company is profitable, where is all the money?"

Cash flow is the net cash inflow (or outflow) that ends up in (or out of) the bank account for a particular period of time. I'm sure you've heard the phrase "cash is king". This is referring to cash flow. It's the amount of money you actually generate over a specific period of time. No matter how large your profit is on paper, most of your business decisions and activities are impacted by the cash that is coming in and out of your business – in other words, by your cash *flow*. For example, your ability to pay a key supplier early to take advantage of an 'early pay' discount will be determined by your business' net cash flow. Do you have the money available to make the early payment?

So, what causes the discrepancy?

Cash flow is impacted by the things you need your money to do and the time frame for doing them. In many businesses, the biggest contributors to cash flow issues are the negative impact that accounts receivable and accounts payable can have on your cash flow. The timing of when you collect your money from your customers is most often days, weeks or months *after* you send your customer their invoice. Similarly, most creditors will grant you time to pay their bills beyond their invoice date. However, the **real** cash flow issue stems from the gap between the time you collect on your accounts receivable and the time you need to pay your suppliers. This time gap can often be as much as 30 or 60 days, which puts a lot of pressure on your cash flow.

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Principal payment of loans is another key contributor to the discrepancy between cash flow and profits. Debt repayments must come out of your profits or you will need to find an alternate source of capital to afford these types of payments.

Two other things that often contribute to the gap between profit and cash flow are the purchases of equipment (capital assets) and dividend payments paid to the owner(s). These expenditures reduce your cash flow by the amount actually spent. In order to minimize cash flow issues, purchases of equipment are often financed by debt to avoid large cash-out lows, and dividends are generally only paid when profits yield the needed cash to fund the dividends.

Many business owners plan for increasing profits but don't spend the time needed on improving cash flow. A wise business owner will devote the required attention to maximize cash flow in addition to (and probably more importantly than) the planning devoted to improving profitability. Profits are important, yes. But even more important is the ability to access those profits with a robust cash flow so you can do what the company needs at any point in time - a key advantage to running and growing a successful business.

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2 Making financial decisions *without* proper analysis

Mistake #2 happens much more frequently than you'd expect. It occurs when you make financial decisions that affect your business *without* understanding the full financial impact of them first.

> Quantify the results *before* you commit to a decision that will impact your business

You own a business to make money, of course. With that clear goal in mind, it's obvious that most of your actions are based on the numerical analysis that ensures your actions will result in a reasonable profit. And while some important decisions are based on nun-numerical factors, in all cases you need to understand the mathematical reality and assess the financial effect before making decisions for your company, right? In fact, the opposite is true.

Often, fundamental decisions are made with a total disregard

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of their effect on profitability and cash flow. I would go so far as to say that ***many*** business owners go about this kind of decision making before they have run the numbers and calculated the impact. Sound silly? Let's look at two examples: pricing your products or services, and determining the compensation to be paid to your employees. Both of these decisions directly impact profits. Did you conduct a thorough analysis of your decisions about these amounts and quantify their effects *prior* to acting on your impulses?

Example 1: Employee compensation

Paying fair compensation to your employees is imperative. Offering a compensation package that attracts and retains talented staff is also important to your ultimate success. However, these factors must be weighed in the context of your business' total financial picture. For example, you simply may not be able to pay the rate you'd like to right now if your available capital and cash flow won't support the numbers. Perhaps you'll have to work with a skeleton staff for a while, or do some things yourself that you'd like to eventually hand off to an assistant. If you absolutely must pay a certain level of commission that isn't feasible at the moment, you may have to find other sources of short term capital or find areas from which to trim expenses - or perhaps live with not generating the level of profit you desire. You can also consider working out a creative deal that ties future commission increases to company performance.

> The numbers don't lie; listen to what they tell you before you make a decision

There are all kinds of solutions available; the important thing is to really look at what it will mean to your company before agreeing to a compensation plan. If the numbers don't work, then hiring even the world's best employee just isn't something you can afford to do.

Example 2: Product pricing

Improperly pricing your company's products or services is probably the ***most*** common mistake that owners make. In particular, many do harm to the company by attempting to increase sales (and presumably profit) by discounting the price. While this sounds good on its face, the mathematical truth is that discounting your products or services is almost never a wise idea as a long term profit-generating strategy. If you offer a discount you will have to sell much more in volume in order to make up the lost profit from the discounted selling price. For example, if your present margin is 35% and you reduce price by 10%, your sales volume must ***increase by 40% to produce the same level of profit.*** And this is without planning for any improvement to profit at all!

Moral of the story: Homework pays off

Discounting your prices to compete doesn't generally make sense from a long-term perspective. Competing by offering excellent value for the price that makes your business profitable, on the other hand, makes a great deal of sense. Likewise, when hiring new people, study the numbers to make sure it is at a level and structure your company can truly afford.

There are numerous other decisions like these that business owners face each day and all of them make a difference to your company's financial outlook. Quantifying the result of decisions that you are considering will help you make choices you can live with. The numbers don't lie; listen to what they tell you before you make decisions that matter to your bottom line and impact your overall success.

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3 No formal business action plan in place

Mistake #3 is the all too common failure to have a formal action plan for improving the business. Many business owners avoid making such a plan without recognizing the pattern this behavior mimics: doing the same things but expecting different results, which, as we all should know, is the definition of insanity. To see change and improvement in a business, as in any other venture, you must change your approach. Only then can you expect to get a different outcome.

In my years of consulting with business owners I observed countless savvy company leaders omit this critical step. I decided to explore their reasons for such an important misstep. Their answers indicate that often they don't develop an action plan because they:

- Don't know how to make a plan
- Don't think a plan is necessary
- Are afraid of the process
- Don't want to commit the time to create a plan
- Think it would be a waste of time
- Believe planning is only relevant for larger businesses
- Believe planning is something done only to acquire a loan
- Believe a plan must be a thick document complete with charts, graphs and well laid out chapters

> "My business is up and running, so why do I need a plan?"

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Many business owners use one or more of these excuses to avoid making a plan but in fact a regularly updated formal plan of action to improve your business is necessary and relevant for ***all*** businesses regardless of size or industry. The reality is that planning can be (and generally is) a simple and effective process – and I stress the word "process". The process of writing down your plan transforms it from a dream based on a vague idea of a desired outcome into a realistic path from point A (your business' current state) to point B (what you want your business to be). Thus, the greatest value of developing an action plan is in the process of creating it rather than the end result. Building a staircase is far more useful than gazing longingly into the heavens and hoping for an updraft.

Ok, so how do you begin?

Creating your plan does not need to be a complicated. An action plan can take the form of:

- A bulleted or numbered list
- An action table
- A list or action table with additional details

The critical thing is to include a description of goals and actions in terms of who, what, when, perhaps why and if necessary, where. Your plan can be focused on your business in general or about any specific aspect, including:

- Operational issues
- Strategic issues
- Financing
- Marketing
- Human resources
- Information technology

Note that although I'm calling it a *formal* plan, an effective action plan doesn't have to be terribly "formal". It merely has to be written down and used as a working tool in your business to remind you of your goals and the steps you are taking to achieve them. Your plan will guide your footsteps as you make daily decisions about things that affect your business, and even how to spend your free time. When you know exactly where you want to go and have created logical steps to get there, you have a much greater chance of reaching your goal.

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What if the original plan isn't quite right?

As you work through your plan, you may find that some steps need to be altered. That's perfectly okay. In fact, this is very useful information that you will only acquire by having a plan and following it. Adjustments along the way let you measure how far you've come and the relative effectiveness of your current plan. I advise my clients to make an action plan on a monthly or quarterly basis and keep it as current as possible. This way they always know where they're going and can adjust both the goals and the steps to achieve them as needed. Little by little, your plan will help you reach your dreams.

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4 Competing on price, not value

Mistake #4 is the decision to compete on price rather than on the value of your products and/or services. I can't tell you how many business owners feel the urge to do this. As a finance guy, this worries me because I understand the significant negative impact that price discounting can have on growth.

I sat with a client once in an interview for a new sales person. The candidate actually said, "The first thing I will do is offer 10% reductions in price to new customers." Wow! I could not believe my ears. Why? Let's look at the math. If, for example, your business operates at a 30% gross margin level and you reduce prices by 10%, your volume must increase by **50%** just to achieve the same profit levels. And I would say that for most business owners, where growth and profit are key areas of focus, this is huge!

> "But if it's on sale, they'll want lots of it!"

In my role as a business advisor, I often hear comments like, "My industry is so competitive," to explain this urge to reduce prices. However, it's not an effective strategy for growth in most cases no matter how strong the surface appeal. Most consumers make their purchasing decisions based on a slew of factors. Price isn't the primary key, contrary to the beliefs of many business owners. In numerous studies of what drives buying decisions, price ranks quite low on the list.

With that in mind, I advise business owners to focus on the actual value of their products or services to the end user. My recommendations with regard to pricing include:

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- Develop a unique selling proposition (USP).
- Create a point of differentiation from your competitors.
- Understand your competitors' prices but not for the purpose of mimicking them.
- Develop proper messaging and communication language to support your USP.
- Train your team to use this language – including outside sales, inside sales and customer service.
- Understand what all of your costs are (both variable and fixed) and incorporate this knowledge as you set prices.
- Develop a forecasted operational model that will yield the level of profits that will meet your goals – pricing must be built into this model.
- Consider discounting as a method to clear out old inventory or as a lead generation strategy, but in the latter case be careful that you do not set a precedent that will be very difficult to change.

Discounting your prices without a very good reason is counter-productive. It could indicate or give the perception that you believe the value you're offering doesn't match up with the prices you've set, and this will act to hurt your bottom line. Instead of discounting, set realistic prices based on your costs and profit goals as well as the value you're providing. Then set out to communicate to your clients and customers why it's a great deal at that price. This may not be easy as it could take you outside your comfort zone but trust me – go for it!

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5 All sales are *not* created equally

Mistake #5: "A sale is a sale is a sale!" Even though I am a "numbers" guy, I have helped my clients develop and connect sales plans to financial plans (and vice versa) countless times. In the midst of these exercises, I often hear this comment or witness sales teams operating with this mindset. This typically stems from a perspective of weakness, desperation, or simply a lack of knowledge.

To put it bluntly, "a sale is a sale is a sale" is just not true. Why? Let's explore:

1. Profit that actually contributes to your business

Most businesses have different product or service lines, each generating a different level of gross margin. Understanding this concept alone – different levels of gross margin – helps to explain why all sales, whether product or service based, are not all equal.

2. Size of sales in terms of monetary value

For a moment, ignoring the individual profit generated by a sale. If that single sale is 10 times larger than the next, which one is clearly more valuable to a company? This demonstrates that sales have different monetary values and, therefore, different levels of equality.

3. The effort and initiatives required to generate a sale are not accounted for in measuring the profit

Realistically, some customers take more time to convert, therefore costing more than others. These sales are not meant to take more time, but a sale that is harder to procure may not be considered equal to a sale that is "more simple" or "easier" when ignoring all other factors.

Do all sales deserve equal attention? *No!*

4. How the customer fits in relation to a company's sales plan

By this I mean, if a business' core service is selling hot tubs, then a sale of ancillary parts to a walk-in customer who already owns two hot tubs may not be considered as important as making a sale to a first-time hot tub buyer.

5. Future sales opportunities

This is fairly straightforward: a sale to a customer with a number of up-selling or cross-selling opportunities is likely to be worth more to a business than a sale to a customer with a limited number of up-sell / cross-selling opportunities.

6. Opportunity for future referrals

Referrals are by far the most cost effective marketing any company can do. A smaller sale to a customer that may provide lots of opportunity for future referrals may be worth a lot more to a business than a one-time larger sale to a customer with no future connections or referral opportunities. Before focusing strictly on the value of the individual sale, try and assess what the potential *future* value of the customer may be.

7. Risk of warranty or after sale service

Large sales to a customer are fantastic. BUT, look to see if a larger sale to a customer has a higher risk of future warranty issues. If it does, than this sale may be considered less valuable than a smaller sale with far less chances of future warranty claims.

While I could go on and provide several more examples of how all sales are not equal, my objective isn't to produce an exhaustive list of examples. Rather, this is meant to get

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you thinking about your business, your sales, and why your team should be thinking strategically about your sales.

6 Blaming poor performance on external factors

Mistake #6 is a human tendency that shows up in all kinds of areas even beyond business. This is the unwillingness to take full ownership of poor performance, in this particular case, the operating performance of the business. It's all too easy to blame a lack of success on factors external to the business.

This has come to my attention particularly over the past few years as multiple clients have attempted to pin their slump on the weak economy or the overall slowdown of their industry. Although I understand the environment in which we are all operating, and I don't walk in my clients' shoes, blaming the economy comes across as an excuse.

It's your job to take control of the *un*controllable

Yes, there are certain elements that will always be outside your control as a business owner. Regardless of how much you may want to have complete and total control of every aspect of your business, the truth is that you will not. There are some elements that are simply bigger than you. Of course many of these factors will affect a business negatively, but from my perspective, savvy business owners try to identify these "uncontrollable" factors and develop business strategies to compensate for them.

> "I have no control over my business; I'm completely at the whim of customers."

For example, I have a client who is in the flooring business. For years, one of his major business segments was selling and installing flooring for home builders. This segment made up about 25% of his total revenue. When the recession hit our local home-building market, my client was astute enough NOT to blame his slumping sales on this external factor.

It was beyond his control, so he had to accept the change in market conditions. Instead of helplessly casting blame at a change that made success unfeasible, he developed a new growth strategy around an expanded client pool with new products. That shift in his own strategy and mindset allowed my client to

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achieve huge growth even through recessionary times that put many people in his industry niche out of business.

Today, the fact that my client used to sell to the home-building market is almost like a distant memory. He adapted to the reality of the market – a factor he couldn't control – to be successful with conditions as they existed rather than failing and blaming the world for not conforming to a reality in which he was prepared to succeed.

Flexible thinking leads to resiliency

This is the kind of flexible thinking that allows good business owners to thrive in any economy context regardless of industry. The world of business is dynamic, and to succeed over the long term you must be prepared to adapt your strategy to fit the facts on the ground. If your business isn't doing well, something needs to change and it is up to *you* to create this change. It may be your business model, your process, your staff or any number of other factors, but the path to success never lies along the path of blaming uncontrollable factors for being what they are.

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7 Not having the right people doing the right things

Mistake #7 leads us to the infamous organization chart. Have you ever looked at your business in the context of your "org chart" to understand why you have it set up the way you do? Is the structure of your business clear and logical? Does it make sense, given how you need to operate your business?

> Understand the roles and skill sets you need to succeed, then find the right people to fill them.

Traditionally, when people are building a company, they look at the individuals they have and create the functions and roles around these individuals. However, this thinking is a bit backwards as it does not take into account the best structure of required functions that would work within the individual company. Rather, it merely focuses on the people available. This leads to a common business mistake: suddenly you have the wrong people doing the wrong things trying to make a business successful. In other words, the road to success is not as straightforward as it could be.

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For example, consider a company that has a person in a customer service role and although the individual may be a great person and employee, they have very poor verbal skills. The person may have been placed in this position without a thorough understanding of the required skill set for the role. It becomes more about the individual *person* rather than the individual *position* and the necessary functions of the position.

Through recent analyses and discussions, I've concluded that businesses that actually thrive in their growth are those that first look at the required structure and roles needed to make their business succeed, *then* find the people with the right skill sets to fill those roles.

A great resource to delve deeper into this concept is Gino Wickman's book, *Traction: Get a Grip on Your Business.* It helps solidify the science behind finding the right structure first, then finding the people skills needed to support the right structure.

In order for your business to function more effectively, I suggest that you take the time to assess your current organization structure in relation to the following:

1. Determine the right "seats" for your company

What are the actual functions that your business needs to operate effectively to grow and succeed? Do not think of WHO your business needs, merely focus on the required functions within your business. This will become the developed STRUCTURE of your organization. Note – this structure may need to change over time as your business grows.

2. Develop the roles for each function

Once you've highlighted the required functions within your business, define the specific roles. This is where you outline the responsibilities and accountabilities within each function. These two items together – functions with their defined roles – become your Organization Accountability Chart.

3. Ensure you have the right people

Once you have a clear understanding of the positions and their responsibilities, find the right people to fill these roles. This can be done by looking at who you currently have within your company and putting them in the role appropriate to their skill set and personality, or you may have to look outside.

If you are looking at restructuring your business, you may find that you have some seats that you do not have the right people for, or people with no seats. In this case, you may

have to hire or eliminate the seat and distribute the accompanying responsibilities. You may also have to let go of the people who no longer fit a required seat within your required structure.

The objective of structuring your business shouldn't be about finding positions for people, but finding the right structure for your business, then filling with the right people. It's about matching the right structure with the right roster of people both in skill set and in personality.

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8 Not understanding the financial impact of operating deficiencies

Mistake #8 results from not understanding just how co-dependent all of the parts of your business are. Businesses are fascinating beasts where everything is interconnected. If you change one part of the "beast", the organism as a whole may experience side effects – both positive and negative.

Unfortunately, in my experience, this is not often realized until a company is forced to do a deep dive into how their company is functioning, particularly when assessing finances. For instance, if a company is determined to increase their gross margin, they may be inclined to simply increase their prices. However, if there are actual operational inefficiencies within the company, then increasing prices will not solve the underlying issue. Rather, the company should consider the financial impact these inefficiencies are having on their business and make the necessary corrections within their processes.

Case study: Connecting the financial impact of operational deficiencies

To illustrate, let me give you an example using a business in Calgary I have worked with for a long time. Over the years we have been monitoring very closely the business' gross margins by each of their major customer segments. During one particular monitoring and planning session, we were forced to look at the financial impact that an operational hiccup, or "deficiency", was having on the gross margin of one of their business segments.

One small change in your business operations can yield large results

Interestingly enough, we found the gross margin in that particular segment was being eroded not by pricing issues, but by operational glitches between scheduling and installation.

What we found

After assessing the business, we found there was a gap in communication within the operations department. The scheduling department, delivery department and installation department were not on the same page, and as a result, there was a "waste" of time happening on many, many individual jobs. This waste of time could not be absorbed by their customers, and rightly so, but instead the cost was eating into the company's gross margin.

Breaking it down

For every scheduling issue that happened, the result was roughly one hour of labour time that was costing the company approximately $100. While this alone may not seem like a huge loss, we decided to look a bit further.

What we noticed was this:

- In one year the company completed about 750 jobs.
- In two-thirds of those jobs there was a breakdown in communication between scheduling, delivery, and installation.
- Doing the math, we found that the company was actually *losing* **$50,000** each year - a pretty significant hit to the bottom line.

This amount would have meant the company achieved their gross margin goal, however it was being lost on something that was within their control. Clearly, we had to take a moment as we recognized that the operations of the company was having a SUBSTANTIAL and DIRECT impact on their bottom line.

Once we determined the issue, we were able to assess why these inefficiencies were occurring and what solutions could be developed. From there, the business was able to implement better internal systems. They improved their margin by improving the communication between scheduling, delivery and installation. **Not only did this improve their gross margin, but their client service improved greatly as well!**

Lesson learned

This was a huge lesson for the client in understanding that the finances were not just about the money. It became about the entire business and all its departments; that to truly understand what impacts a company's bottom line, one must take a hard look and

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recognize the impact that one department can have on a seemingly separate, independent one.

The connection between finances and operations recognizes that subtle influences can have a substantial impact on a company’s bottom line - crucial to understand in any business.

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9 Lack of processes to manage and maximize cash flow

Mistake #9 is actually an extension of Mistake #1, which was not understanding the difference between "profit" and "cash flow". Now that you understand the difference, let's look at cash flow more closely.

If you want your "cash" to flow, as suggested by the term itself, it's your responsibility to consistently monitor it and take action to keep the "flow" moving. Seems straightforward, I know. But this “consistent monitoring” and “action” are often the bottleneck of a business’ cash flow. Wouldn't it be best to have proper systems and processes in place to keep everything flowing smoothly?

Managing cash flow can be as simple as understanding what factors impact your business’ cash flow and how, and then effectively managing those factors. Factors could include issues such as when sales invoices go out, when you pay your suppliers, when you follow up on invoices, invoice payment terms, and the list goes on. Each of these is a factor that you can control (to an extent) and develop processes to ensure they all complement one another in a way that positively affects your business and its cash flow.

Cash flow isn't a once-a-month item for review... it's daily!

Common cash flow mistakes

In my experience, there are six common areas where a business can first look to help improve its cash flow. Take a look and see if any of these are happening within your company to negatively impact your cash flow:

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- **Time gaps:** There is too much of a gap between when your product or service is delivered and when the invoice is actually sent to your customer. This could increase the likelihood of customers taking longer to pay you, as well as increase the risk of not invoicing for work at all (although this is slim in most businesses). By setting up a daily / weekly / bi-weekly invoicing process, you are more likely to capture all completed projects and have them paid in a timely manner. It is also recommended that you make it as easy as possible for your customers to pay you (e.g. accepting credit and debit cards, direct deposit, and so forth). If you prefer to have your customers pay you via a cheque, that's fine, but be sure to deposit the cheques on the day you receive them and not have them sit in a deposit book for days on end. In today's world, e-transfers are quite common in many small businesses.

- **No defined follow-up procedure:** While your invoice may go out in a timely manner, there is no clear structure in place for when and how to follow up with unpaid invoices. Does your company follow up at the 15-day mark? Before the 30-day mark? Is it via email, phone call, or in person? Or is it a combination? Who is responsible for the follow-ups and what happens if it needs to be escalated? Make sure these questions have clear answers. Let your customers know up front what your procedures are to remove any misunderstanding around invoicing and payment expectations.

- **Timing of vendor payments:** Do you pay your vendor invoices at the same time you send out your customer invoices, depleting your bank account? How are you managing when you are paying your suppliers versus when you are getting paid by your customers? Is there a system or process to ensure that your customers are paying you first *before* you have to pay your vendors? Having these processes in place allows you to proactively monitor and manage when money comes *into* and goes *out of* your company. You'll improve your cash flow by mitigating or avoiding moving into a debt scenario. Sometimes this cannot be overcome, but you can at least start by paying attention to the timing of when you pay your vendors relative to when your customers are paying you.

- **Investment in your inventory levels:** Are you effectively managing how much inventory your business is putting on its shelves? Do you have too much inventory relative to your sales levels? Is your inventory turning over too slowly? If you are not effectively managing your inventory levels, this will not only negatively impact your cash flow but it will also put your business at risk of losing money on inventory that becomes obsolete or without value and cannot be sold at all.

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- **Required debt repayments:** Debt repayments have to come from either after-tax profits or other forms of debt. If your levels of profit are not sufficient relative to your debt structure, your business will start to have cash flow issues (subject to an injection of capital) and may soon require you to implement the not too uncommon strategy of "robbing Peter to pay Paul".

- **Investment in capital assets:** A common error many business owners make is using operational cash flow to purchase capital assets. This causes undue hardship on cash flow. One of the first things you learn in Financing 101 is to finance capital assets using long-term financing, *not* operational cash flow. A great example would be purchasing a piece of equipment or a truck by writing a cheque from your business bank account or line of credit, as opposed to using a term debt facility that better matches the payment terms with the life of the respective asset.

Where to start

Starting to effectively manage your cash flow can be daunting. I recommend asking yourself the following questions and moving forward based on your answers.

1. Do you understand what is driving your cash flow?
2. Do you understand which activities you should be undertaking to have a better impact on your cash flow (e.g. more invoicing frequency)?
3. Do you know what required activities you are currently *not* doing that should be done for better cash flow?
4. Are you and your team willing to "roll up your sleeves" to complete these identified cash flow management activities?

Once you've answered the above, you have a starting point for the day-to-day activities required for proactive cash flow management. A lot of businesses are not aware there really is NOT a silver bullet that will help improve cash flow. It's about implementing a number of tactical items that need to be completed daily and monthly to help improve cash flow.

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10 Not recognizing the *Six Drivers of Profitability*

Mistake #10: The belief that **one** drastic change is all it takes for improved business growth. Not quite…

Having worked with a multitude of business owners, my most successful clients have found the opposite to be true; that improving the bottom line isn't about making one major change within their business. Rather, to have long-lasting positive impact on the bottom line, it is important to understand that change happens in small, incremental steps in six different areas. These areas are known as the **Six Drivers of Profitability**.

In fact, it is actually through small, incremental changes to several of these six areas that substantial transformation to your bottom line will be made. As a business owner, you will bring about growth by making subtle improvements to different areas of your business, as opposed to looking for that magical or fictional silver bullet that very likely does not exist.

So, what are the "Six Drivers of Profitability"?

The key to making change is to fully understand the six areas that actually influence your bottom line and recognize how they interact with each other to positively affect your business.

1. Average price

Fairly straightforward, this is the *average* price of all of your products or services. Simply increasing the price of your products or services may or may not lead to an increase in your bottom line – you will need to consider both the potential for customer loss and drop in sales volume in this equation. Furthermore, do not think that offering discounts to your customers will yield greater sales and result in an improved bottom line. As a growth strategy this rarely works given the huge sales volumes that need to be generated to compensate for the effect of the discount. In fact, the price of your products or services is actually highly influenced by the next driver, the average transaction size.

Small improvements in these areas can bring big growth to your bottom line.

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2. Average transaction size

This is simply the number of units per transaction. Your average transaction size combined with the average price gives you have the **Average Transaction Value (ATV) -** in other words, the average *value of a sale***.** The value of the sale is what truly matters, not the price or size alone. Upselling and cross selling are two key strategies that can allow you to increase your transaction *size* without having to increase or change your selling *price*. Remember the infamous question, "Would you like fries with that?" If *this* upsale can be successful, then likely any business can be successful!

3. Number of transactions

The number of transactions (#T) is a function of the number of customers your business serves and the frequency in which they buy. It's important to focus on the number of customers your business serves and the frequency in which they buy from you. Do not simply focus on **new** customers; instead sell more to your **existing** customers. It's always easier to increase sales with existing customers than it is to convert a new one.

This, in combination with the ATV, gives you your total revenue (TR):

TR = ATV x #T

An example: Let's say that your ATV is $30 and you have 50 transactions at that price. Your TR will then be $1,500.

TR = $30 x 50
TR = $1,500

Great! You have revenue of $1,500. However, your actual profit is not this number, simply because of the next three drivers – the ones that actually cost your business money.

4. Costs of goods sold

What did the product actually *cost* your business? Think in terms of what you paid the manufacturer for the product or your labor cost to supply or install the product.

Costs of goods sold (CGS) are actually a variable cost as they change with the volume of revenue. In determining what your gross profit (GP) is here, you will have to determine the difference between total revenue and total costs of goods sold.

GP = TR – CGS

5. Direct expenses

Depending on the structure of your "books", you may or may not have these types of costs segregated. They may simply be part of your overhead costs.

A firm grasp of the six drivers equips you to navigate any market.

Direct expenses are overheads that are directly associated with, and can easily be traced to, revenue-generating activities. Examples of a direct cost are selling costs, or commissions to your sales people. Often these costs are treated as overhead costs in your books, but truly these are a direct expenses. The more you sell, the more you will pay in commissions.

6. Enterprise overheads

These are expenses that are neither costs of goods sold or direct expenses, but are still necessary for running your business - think office space, technology, and so forth. Often these are referred to as "General and Administrative" or simply "Overhead Costs".

Putting the pieces together

Once you understand how these six variable drivers work together and what initiatives work best together to drive results, you should then be able to see small steps you can take in the business to improve your profit. It’s about recognizing how these six areas influence one another so that you can work *smarter*, not harder, to improve your company’s bottom line. You don’t need big improvements in any one area; you need small improvements in multiple areas. This approach gives your business a better chance at improving your profit margins without becoming overwhelmed by changes.

Just because something works for you one year doesn't mean it will work the next. Having a firm grasp of the Six Drivers of Profitability equips you to navigate any market. By understanding the subtle influences, you will be able to know what is best for YOUR business within a specific economy.

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11 Lack of leadership to guide and empower the team

Mistake #11 is based on the fact that being a business owner requires you to be a leader. A while back, a client of mine told me that his son said to him one day, “Dad, your employees are people. They are not robots, so they need to be treated appropriately.” As this was quite a philosophical statement coming from a young man with limited business experience, my client took stock of what his son had said.

While not an unsuccessful business owner, one of my client’s strengths, prior to this comment, *wasn’t* delegation. Once he realized what his son was saying, he assessed how he could not just treat his employees better, but actually *empower* them so that:

1. they would grow themselves, and
2. he could actually step back and focus on the bigger picture of the company.

> The success or failure of a company is generally a function of who's at the top.

Over the next few months, I saw a distinct change in how my client dealt with his employees, and I watched him become one excellent leader…not just a business owner.

What do I mean by “leader?”

“Leader” has a plethora of definitions tied to it. In fact, a simple Google search of the term brings up pages of different definitions – all with slight variations. For the purpose of this article and what I saw in my client as he became a truly great leader, below are the attributes that I believe make a quality leader within an organization.

1. "Guide", but don't "do"

In other words, simply teach your employees the skill set required to do a role, then step out of the way and let them do their job. Be there to listen when they have questions and point them on the right path, but don’t perform their role for them.

2. Be supportive

What your employees will be able to achieve knowing that you support them – their talents, their judgement, their growth – will go a long way to not just seeing your company grow, but to seeing employees become vested in their own positions. A few ways to show your support include:

- Standing up for employees when required and not “throwing them under the bus” when something goes wrong.
- Empowering them to succeed – giving them the tools to make good decisions on their own.
- Motivating them based on their own individual motivators.
- Encouraging them to be their best while allowing them to learn from their mistakes, rather than simply giving up.

3. Listen to employees’ ideas AND concerns

Taking the time to understand what your employees are actually saying, whether good or bad, demonstrates that you are willing to grow based on their feedback. To let your employees know that they are being heard:

- Talk ***to*** them and not ***at*** them.
- Be compassionate / sympathetic to their concerns, yet firm when you require forward movement, whether in a decision, specific project, or something else altogether.

4. Show patience, yet be proactive at the same time

Let your employees air their issues and concerns in a supportive environment, but turn the conversation to solutions, rather than dwelling on a problem.

5. Take responsibility / accountability for the whole company

This is *your* company, so *you* are ultimately responsible for everything that happens within it. Stand by your company.

6. Understand that you may not know everything and be willing to learn

The greatest leaders willingly admit what they don’t know. They become great because they can admit this, then take action to surround themselves with people who fill the knowledge gap. Empower your employees to become experts in their roles and rely on their expertise to help you guide the company. Build your business on everyone’s strengths.

When those at the top possess great leadership skills, the journey to success is quite a bit smoother.

7. Be realistic of your expectations for your employees

Remember that while this may be your business, your dream company, for most of your employees this is merely their job. Know that they will not be as vested in your business as you are…and that’s okay.

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8. Actions speak louder than words
A great leader isn't just about talking the talk. Rather, as a leader, take the time to *do* what you say you are going to do, and when you say you are going to do it. Lead by example, not by command.

One of the most important things you can recognize as a business owner is that, in a business organization, the success or failure of a company is generally a function of who's at the top. When those at the top possess great leadership skills, the journey to success is quite a bit smoother. Ask yourself, where are you at with these specific qualities?

12 Not articulating the vision for your business

Mistake #12 grows out of that old saying, "If you don't know where you're going, how will you know when you get there?" If someone were to ask you what your company's vision is, would you have a clear answer?

> "If you don't know where you're going, how will you know when you get there?"

First, let's understand what a vision is and why it's important to have one. The term "vision", in the context of business, can be convoluted. Some define it as "the optimal state of the business", but I don't believe this is concrete enough.

To me, a company's vision is simply ***where you are trying to take your business***. This allows your vision to become concrete, defining exactly what you want your company to look like and how you plan on getting there.

Regardless of the actual definition you choose, it's absolutely critical that you know exactly where it is that you want to take your business and that you can actually *articulate* it to anyone who asks. In fact, it is even more important as the leader in your business to actually let your employees and colleagues know where you are headed.

Why is this important? Simple – if you don't know where it is you want to go with your business, how will you know when you get there…or even *if* you get there?

By clearly defining your vision, you can build measurable metrics – financial, operational, and interpersonal functions – that can act as guides for your business growth. Really, your business planning should be directly connected to your vision, and your vision to your planning. Your vision will help guide your business plan and keep you focused throughout your weeks, months, years, even decades as a business.

Being able to clearly state your vision to others is akin to why experts say you should write down your goals **–** if they aren't written down, they're not goals, they're simply dreams.

By ensuring that your entire team understands your vision, you also give them insight into what the purpose of the company is and how their role can directly affect the company. When your employees understand your vision, they can then better answer their own internal questions of:

1. Why do I want to work here?
2. Should I actually work here?
3. Why do you, the business owner, do the specific things you do?
4. Do I truly fit in with where this company is and where it is going?

When your employees understand your vision, you empower them to understand if your company is the right place for them. If it is, then these employees become more invested in your company because they see the link between their contributions and where the company is headed. If they decide your company *isn't* the right place for them, they will choose to leave **–** which also benefits your company.

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About the author

As a Chartered Accountant and external CFO since 1986, my passion for business runs deep. I understand the challenges that business ownership brings and I thrive on helping my clients recognize and overcome those challenges so they can move their business forward *profitably* with confidence.

I started out as a traditional accountant in Calgary, but it wasn't long before I realized my desire to provide business expertise at a more strategic level, beyond being the "year end guy". In 1996, I launched BusinessWORKS to do just that. My greatest source of pride comes from my clients' successes and the long-lasting relationships I have built with them through this work.

Outside the office, family time is front-and-centre with my wife Nicky, son Spencer and our dog Dexter. I am a devoted Saskatchewan Roughriders fan, and love playing and watching hockey about as much as I love business.

If any of the issues I've covered in this report resonate with you and you're ready to get to the bottom of addressing them, I invite you to get in touch with me. You can reach me at 403.228.2535 or email steven@businessworkscas.com.