

ExpertAnswers: Expert Tips for Financial Management



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All small businesses have something in common: a need to fully understand financial aspects such as budgets, cash flow, pricing and balance sheets. Otherwise, entrepreneurs may not fully understand what's happening with their business until it's too late.

Lou Davenport, a SCORE mentor for over 14 years, has helped hundreds of small business owners develop basic financial management skills that lead to success. Read his advice on how you can master your numbers.



You've no doubt counseled many aspiring entrepreneurs who were apprehensive or intimidated by the financial aspects of running a small business. What can help them become more comfortable with this all-important facet of business ownership?

If you were to spend a long time in another country, you'd have a difficult time getting by if you didn't know the language. The same is true for being an entrepreneur in a new business environment. You need to understand what financial reports are about, interpret them and use that information for sound financial planning. Not doing so puts the survival of your business at risk. It also gives your competitors an edge because they most likely know how important financial reports are.

What are the keys to effective short- and long-term financial planning?

Typically, small business budgets are planned for one year, while long-term financial planning should be done for up to three years. SCORE offers some great [Excel spreadsheet templates](#) with built-in formulas that can help you prepare pro forma forecasts for up to three years. Once you learn how to use what-if scenarios, you can better analyze, track and compare business results. You can then use first-year projections as your budget, tracking things as you go along.

Coming up with any kind of budget may be difficult for a start-up with no previous experience. How does one make accurate projections without this experience?

SCORE templates can be helpful here also, because they provide various expense categories for start-up and ongoing operations. While they will help trigger your thinking, it's a good idea to review your projections with a SCORE counselor. Having likely worked with many different types of businesses, he or she can serve as a third party to make sure you've covered everything accurately. That helps make your job easier.

What are some frequently overlooked considerations in small business budgeting and financial planning?

A common reason small businesses fail is because they run out of money. And this is often due to new business owners not paying enough attention to their balance sheet and cash flow forecast. For example, you may determine that \$30,000 will get a business started. But if it takes a year and a half to break even, it may well cost another \$30,000 to reach that point and become profitable. Not recognizing and planning for these situations by failing to track your financial data is a fatal error that may cost you your business.

What do you consider to be the most critical financial statistics to monitor and why?

The most important financial statistic to monitor is Gross Profit Margin as a Percentage of Sales. Here's why:

1. Sales alone aren't real money. You can't pay expenses with them.
2. If the standard for your industry is 40% and you're only at 30%, you have a serious problem. You're either pricing poorly, making inaccurate cost estimates or working inefficiently.

Free Business Resources

10 Bookkeeping Basics You Can't Ignore

Know Your Numbers: What You Can Do Now to Drive Stronger Financial Health

Small Business Financials: Smart Ways to Get Paid Faster

Collecting on receivables is a common challenge for small businesses. What are some ways to prevent late payments from becoming an issue and affecting cash flow?

You have to be persistent, consistent and insistent. This is not the most pleasant part of owning a business, but you have to be disciplined enough to regularly push late-paying clients and take a firm stand on what they owe you and when they have to pay it.

Collection tends to have a negative, confrontational implication. Are there more positive, non-confrontational ways to get customers to pay what they owe you?

Establish a clear understanding with your client up front on the terms and conditions of sale, including everything from cash discounts for early payment to fees for being late. It's much easier to set and agree on the payment ground rules at the front end of the transaction than to try to collect later on.

What are some tips for setting a sound pricing structure for your products or services?

1. As noted above, understand the industry benchmarks for Gross Profit Margins for your business.
2. Remember that prices are market-driven, not cost-driven. It doesn't matter what your costs are because the market doesn't care. What matters is if you can make a profit at the price the market will bear.
3. Don't underprice when you're starting out. Many businesses try to do this in order to get a toehold when, in reality, they're giving their competitors an advantage. There's no way you can survive for the long term and meet your clients' expectations by pricing under the market. Instead, set prices based on what the market will bear.

How often should you review your pricing structure to ensure you're staying abreast of cost fluctuations?

You should review your pricing structure constantly. In today's world, pricing is transparent. Prices and pricing factors are available on the Internet. It's essential to regularly research pricing factors specifically for your type of business.

Existing small business owner may think they already know all the in's and out's of accounting. But are there new things they can learn or do as well?

Sit down with your financial advisor or SCORE counselor every quarter to six months and go through the financial reports. There is value in getting the perspective of someone who follows things that you might not. And because SCORE counseling is free, you have nothing to lose.

Is a CPA always needed to help with your accounting and financial needs?

A CPA is not always needed for routine bookkeeping. There are services that can do it efficiently and accurately for a reasonable cost. A CPA can be very helpful with your tax returns as an advisor, but don't consult with your CPA only for taxes. They offer many other services and perspectives that can benefit your financial management and planning.

What's the best piece of advice you can give a small business owner when it comes to financial management issues?

Learn to push yourself out of your comfort zone into places where you're not completely comfortable. You'll find that small business financial management is not rocket science. It's actually quite learnable. By learning basic financial management skills, you can learn what the numbers mean, why they're important, and what you should do about them. By doing this, you can put your small business in the position to succeed.

Want more financial management advice? Get **free, confidential mentoring** from **SCORE experts** today. And get more helpful tips and strategies delivered to your inbox by subscribing to **SCORE newsletters**.