

PREVIEW

SMARTER STORES

**Automotive Processes,
Controls & Profitability**

Published by APD



SHOW ME THE MONEY!

Your most comprehensive guide to how automotive dealers can maximise business performance in today's marketplace.

Fundamentally structured around the dealership's processes and Key Performance Indicators, **Show Me the Money!** offers a jargon-free, step-by-step guide to the process of applying Key Performance Drivers and best practices to implement change across a dealership or a particular department and increase performance and profits.

The essential book for a manager to make more profit in the retail automotive sector.

The difference between a profit or loss in a dealership depends upon very marginal differences across many activity and performance variables. These range from how many vehicles are sold and serviced, whilst keeping a loyal customer base, through to minimising departmental and overhead expenses. This requires the ability of managers to lead a team of motivated people in a fast-changing business environment where managerial knowledge and skills are vital ingredients for success.

This book has been written to enable managers and their teams to understand and improve critical financial and operational processes. It comprehensively covers finance, sales, aftersales, operations, marketing and leadership with detailed explanations and best practice.

Through this book a manager can acquire or enhance their knowledge of how an automotive dealership operates, and understand the key principles covered within it. Acting as a working manual the book becomes an indispensable tool to create a foundation for a truly successful dealership.



Dealer principals

Show Me the Money! can support dealer principals with the dealership's business performance plans. They can use this book in the following ways:

- As a cross-reference to examine each functional area and assess its potential to generate increased sales and profit opportunities.
- As a guide to broaden their leadership skills to assist department managers in the rationale and implementation of improvement plans.
- As a gauging tool for the dealership's overall financial ratios to help them steward the business's financial health.



Dealer department managers

Show Me the Money! is an invaluable guide for dealership general managers and department managers to help them maximise the potential of their own department and, in doing so, support the overall business. This book can help them:

- Resource best practices and business principles to increase their department's results.
- Gain an understanding of the priorities of other managers and how their departments inter-relate.
- Gather a good grounding on how a dealership operates, how to lead a team and how to develop marketing plans and drive profits.

Dealership staff

Whilst the primary audience for this book is at a managerial level, Show Me the Money! can also serve as an introductory guide to any member of the dealership team. Whether for those completely new to the retail automotive sector or existing staff members looking to move into management. This book offers them:

- Goal-driven chapters on how to increase performance across each department.
- Detailed diagrams illustrating key processes and KPIs.
- Easy-to-follow explanations of the financial and operational procedures in a dealership.



Original equipment manufacturer (OEM) managers

Show Me the Money! offers a thorough insight into the workings of a car, motorcycle and commercial vehicle dealership, providing OEM managers with a quick comprehension of the range of activities and challenges dealerships face. Therefore, this book is a valuable resource for gaining greater interaction with their network.



Recent reviews on Amazon include...

"I bought this book for my sales and service managers to help them put in best practices to make us more money. They've got stuck in reading it and feedback so far has been very positive. The proof will be if they put in place what they've read!"

"Just been promoted as Aftersales Manager for a PLC. Bombarded with reports and figures. Bought this to help me understand the key finance numbers and how my job can change them. Really useful so far and will share with my team when I'm done reading it."

"I'm new to being an Area Manager for a manufacturer. I needed to get up to speed quickly with how a dealership operates. Luckily I came across this book which has given me all the info I need as background to my meetings with retailers."

"I've bought this for my managers to read as I got tired of having to explain what our KPIs are and what they need to do to improve them. Most of them have now got it! Saved me a lot of time and they now have on hand something to refer to in case they need reminding again."

"I bought this to help my manager's understand the financial KPIs for the business. It's got all the relevant financial measures plus even more information on operations for each department. Really helped them understand what's required to drive profitability and how to manage their departments."

Read on to find out more...

SHOW ME THE MONEY!™

Automotive Processes,
Controls & Profitability

Published by APD

Show Me the Money!

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SHOW ME THE MONEY!™

Guide on how to use this book

The purpose of this book is to enable the reader to gain an understanding into how an automotive dealer operates and to use this knowledge to identify where they can take action to improve their own dealership's financial & operational performance.

It is intended as both a reference and a manual of automotive dealer operations – be it a car, motorcycle or commercial vehicle dealership. It is a reference book to facilitate researching any aspect of running a dealership and, a manual as it comprehensively covers the key areas of the business with an explanation of each business function with best practice noted.

Of note is the move by manufacturers from the traditional franchise model towards an 'agency' business format for their networks. It has yet to be seen what is entailed within an agency structure and the extent to how successful it is for each brand. What is certain though, is that major changes to how dealers operate will be inevitable and that having effective managers and dealer staff will be paramount. Through covering the business fundamentals and best practice this book will help such teams thrive in an ever-changing environment.

The main objective of the book is to assist managers in their drive for greater performance & profits. Specifically, it does this through aiding their development and understanding of the dealership's

Show Me the Money!

processes and measures (Key Performance Indicators), and thereafter, which related improvement actions (Key Performance Drivers) and best practices to implement to achieve results.

For a dealer principal the book can support their own dealership performance plans. First as a cross-reference to check each functional area is fully examined to maximise its opportunity to generate increased sales and profit. Secondly, the book can support their leadership of department managers in the rationale and implementation of their improvement plans. Finally, the dealership's overall financial ratios will be a focus area to ensure the ongoing financial stewardship of the business.

A department manager's first area of interest will be their own department to support their responsibilities to the business. Thereafter, they may wish to review the other chapters to gain an understanding of the priorities of other managers and how their departments inter-relate. For managers aspiring to a dealer principal position, the book makes essential reading as it provides a grounding in:

- How a dealership operates
- How to lead a team
- How to develop marketing plans and drive profits
- How to interpret and use financial and operational KPIs

Whilst the primary audience for this book is at a managerial level, it can also serve as an introductory guide to any member of the dealership team. Whether for those completely new to the retail automotive sector, or existing staff members looking to move into management. The book is designed to be accessible to all. It covers detailed information that can be read progressively for an individual to gain an understanding of the department they work in and thereafter, the overall financial and operational procedures of the dealership as a whole. Finally, for those working for automotive manufacturers, the book provides a thorough insight into the workings of a motor car, van and motorcycle dealer enabling them to readily understand the range of activities and challenges dealers face. Thereby acting as an invaluable resource tool.

Whatever your role, we wish you every success in using this book to identify growth strategies for your business.

Introduction

Show me the money!

This was the popular refrain in the movie Jerry Maguire that Cuba Gooding Jr as the client implores Tom Cruise as the agent to repeat back to him in highly memorable scenes. Cuba doesn't care that Tom Cruise is on his last chance as making it as an agent, he's not interested whether Tom is a nice guy to hang out with, nor about all the future promises Tom makes about his long-term playing career. He just wants the certainty of money now.

What's this got to do with the retail motor industry? Well, how many times has a dealer manager sat through a presentation on a new initiative and thought that what was being proposed was all very worthy but at the end of the day, is this going to be an additional cost with no tangible benefit – or will it make the business more money? And heaven help the person presenting saying the line about 'it will only take selling one more used unit a month to pay for it.' Enough said.

This book could be judged in the same way. Will it make a dealer more money or be an expensive paperweight or gather dust next to a training manual left on a shelf? We'd like to think it will do the former and for it to be an essential manual for every aspiring dealer manager. Plus, it may even teach or remind a few practical steps for generating additional profit to the more seasoned professionals in the industry.

Explaining how the book is an investment and not a cost, it pays to look at the current business environment and the seismic changes occurring. Currently several manufacturers are contemplating selling online with dealers being the delivery agents, there are new entrants in the used car market with direct to customer offerings and electric vehicles are transforming the aftersales sector requiring less servicing, parts and consumables. Combine this with the proliferation in products and brands, ever increasing brand standards and industry consolidation, and it would be a brave person to predict what the future in even the short term will look like. However, there is a pressing need now to support managers in a greater understanding of how to run their departments to the best of their abilities. Furthermore, whatever business models come to fruition, their performance will still depend on the people required to lead and manage their teams to deliver consistent financial returns.

Top performing managers are defined by knowing how their departments operate with robust processes and effective controls. They also know their department measures, how they're derived,

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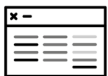
what they show and what processes affect them. Finally, they have the leadership and interpersonal skills to get the best out of their teams.

This book has been written to be a working manual for automotive managers helping them to achieve more in an increasingly demanding marketplace. It can be resourced either in total covering how to operate an automotive dealership as a whole entity, or selectively by business department or function. In a practical plain-speaking style, it covers each business concept detailing the salient learning points and crucially what steps are required to improve the business and effect change.

We respect that you the reader will judge for yourself if we've 'shown you the money' - noting that your investment in this book has been a lot less than the gross profit on one unit a month. Whether we have or haven't, we welcome hearing from you. Ultimately, it will be what is implemented from the principles in this book that will determine its value and we wish you every success in this application.

APD Group Ltd products and services

At APD, we partner with manufacturers, distributors, and retailers to enable them to think better, perform more effectively and sustain growth. We conceptualise, build and deliver agile, fully tailored business management solutions that mitigate risks and increase profitability. Our products and services are:



iCIS

APD's iCIS performance management system is a market-leader, configurable reporting solution that generates a fact-based monthly overview of your franchise network's performance. It enables you to identify any retailers needing triage, territories presenting growth, market trends, and subsequently, to support your franchise network and drive more value out of it.



ProfitPlanner+

APD's ProfitPlanner+ standardises individual budget projections and presents them in a cohesive workflow, creating transparency, consistency, efficiency, and providing a clear picture of the business's financial position. In addition, it simplifies the process of evaluating if franchises are staying within budget by aggregating data from multiple sources automatically, without the need to rely on spreadsheets from each area to gauge performance.



Composite Interrogator

Composite Interrogator is an entirely self-service tool, which empowers organisations to drill down into clearly defined data and access critical insights. It allows you to create the report you need when you need it, granting you access to pertinent information for spotting opportunities and making fast decisions.



Executive Insight

At APD, we work closely with your organisation to create real-time dashboards that are fully configurable to support your individual business needs. Our dashboards can be tailored to include specific metrics, data, or KPIs to help you identify opportunities, overcome a particular problem or optimise performance in individual areas across the organisation and franchise network.



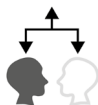
Business Management Training

Offering a range of training courses for managers and customer-facing staff to ensure they have the knowledge, skills and aptitude to meet customers' needs in a constantly evolving marketplace. Courses cover leadership, financial management, sales and service operations and processes. Delivered through a blended approach of training room and online with the capability to be tailored to an organisation's specific requirements.



Software and Data Interpretation Training

A suite of courses to cover in detail APD budgeting and reporting software solutions to enable you to input, extract and analyse data effectively to maximise profitability.



Consultancy

Our business management services can help you develop breakthrough strategies and drive change to improve efficiency in every facet of your business significantly. We put a team of high calibre business management specialists at your disposal, who work with you on implementing best-practice strategies that accelerate growth and expansion, help support transitional periods, facilitate restructuring, and manage change.

If you would like to know more about how APD can support your profit improvement Initiatives, contact us on 01793 832660 or email training@apd-bm.com

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Business Management

1.1 Introduction

Profit and stability are the two overarching objectives of any business, whether it's a quoted company, privately owned or a partnership. All other goals are subordinate to these. A well-crafted marketing strategy may support the attainment of a profit objective but ultimately, without a positive financial return and the creation of shareholder value, such strategies will eventually fail.

At a conference some years ago, an American car dealer and recognised industry expert proclaimed that customer service was the pathway to corporate success. It was then pointed out that one of his franchises, a US domestic brand in terminal decline, had lost 20% of its market share and was now losing money for its retailers. Asked for his response, the expert immediately pledged to slash his franchise's fleet of courtesy cars. The irony was not lost on those present. Without profit, all else collapses. A successful courtesy-car strategy is as much a consequence of profitability as a cause. This is not to say that a sound human-resources strategy or an efficient IT strategy aren't fundamental parts of a business. They are obviously important, but they are all inputs – drivers of success.

Profit is the outcome. Profit provides a reward for risk, funds for expansion and, when translated into shareholders' funds, it gives stability and control.

Therefore, it's only appropriate that this book starts by looking at the measurement of profit. This chapter examines the basic principles of profit, including Net Profit before Tax, Return on Funds Employed, investment, the difference between profit and cash flow, and the business value to shareholders. It also explores the individual elements of the balance sheet and their key relationships, including gearing and working capital. More than most, the retail automotive sector needs to grasp these principles. The margin on which the industry operates at net-profit level can be measured in single-digit percentage points, and low single digits at that. An error in judgement, such as the overvaluation of used car stock or unforeseen external circumstances, can have dramatic and damaging consequences for a dealership's viability. The use of controls and a management team that appreciates the need for them is therefore vital. Daily operating control documents and frequent

performance review meetings based on quantitative and qualitative data should be key features of modern dealership management.

All of these principles apply to all automotive sectors and business formats, specifically with the advent of the 'agency' model, since the need for a viable and profitable distribution channel is crucial, regardless of structure.

1.2 Current situation analysis

At any stage in the business' life cycle, both shareholders and managers need to know how the business is performing against their aspirations. It's a constant process of examining the current results, assessing the marketplace and evaluating the dealership's capabilities so it can adapt and be relevant to its customers' needs. An accurate understanding of its strengths and weaknesses enables managers to prioritise and implement changes to optimise the desired outcomes.

Key considerations include:

- Is the dealership the appropriate size for the level of market demand (opportunity)?
- Are premises and fixed assets the right size to match demand?
- Are sales volume and the associated gross profit sufficient to cover fixed and variable costs?
- Is the management team capable of making strategic, investment and tactical decisions?
- Is the pricing strategy relevant for the market?
- Is the investment in fixed assets and working capital large enough to support the size of the dealership?
- Does the dealership have the right level and balance of stock to support sales volume?
- Does the dealership employ sufficient skilled staff?
- Are the overhead expenses sustainable and more than covered by the direct profits of the operating departments?
- Is the dealership funded appropriately, with the correct balance of internal and external funds?
- Are effective policies and procedures in place and correctly managed?
- Is the dealership compliant with all relevant legal, financial and industry standards?

These considerations are crucial in an industry such as automotive retailing, which is characterised by low margins and market volatility. Examination of current operational performance in this way is called current situation analysis and this chapter expands upon the areas that should be reviewed to

achieve this. Qualitative and quantitative data sources that inform key performance indicators (KPIs) are explored, along with the types of actions that help to optimise them. This enables clear insight into how the current position can be improved to secure sustainable growth and increase returns.

1.3 Key performance indicators (KPIs)

Key performance indicators (KPIs) allow managers to monitor, guide and develop a business over time by identifying current and historical outcomes and comparing this data internally and against other similar businesses and industry averages. The answers to many questions about different aspects of a dealership's performance can be explored in an organised, systematic way using the appropriate KPIs.

For example, a business may be profitable, but determining precisely how profitable is only possible by employing a defined measure over a given period. So what measure of profit should it look at and over what time span? Is it Gross Profit, Operating Profit or Net Profit before Tax, and is it over a month, a quarter or a year? Section 1.10 explores which KPIs to use for different scenarios. The most frequently used profit KPI is Net Profit before Tax %, which shows how much profit is being made as a percentage of net sales i.e., the invoiced sales of the business (section 1.10.1 has a more detailed definition of this KPI).

In many cases, KPIs measure the financial health of the business. There are, however, some that contain no financial measures. Examples would be New and Used Retail Units Sold per Salesperson, or the Ratio of Used-to-New Vehicles Sold in each period. Nevertheless, although these do not specifically assess financial performance, they are fundamental measures of the output of commercial activity. Neither do KPIs always deal with objective measures of performance – they can also relate to subjective criteria. For example, the customer satisfaction indices employed by all automotive manufacturers are based on the subjective evaluation of customer service provided by the dealership, usually by all three main departments. These can be a combination of quantitative (e.g., using an assessment measure or rating scale) and qualitative (e.g., open-ended questions that invite comment – often a rich source of feedback).

In summary, KPIs measure the activities that are the lifeblood of a business. Usually expressed as a ratio or percentage, they show what the dealer has achieved or could achieve, and are enormously powerful tools for measurement and management.

1.3.1 KPIs and benchmarks


While a benchmark uses the same definitions and format as a KPI, rather than indicating what has been achieved, it's a statement of what 'should' be achieved.

Benchmarks are often set by manufacturers or industry bodies to establish standards – they can be seen as aspirations or norms for any participant in the industry and, as such, are powerful tools for raising the level of overall operation's performance in any key given area. In the motorcycle industry, for example, parts sales would be broken down into parts, accessories, merchandise and rider equipment for both revenue and gross profit. Benchmarks for these are very much brand-driven, and reference to composite data (see section 1.9) is the best source for comparison.

The principal KPIs and benchmarks for the overall measurement of a dealership's performance are a matter of debate. Many brands specify precise KPIs for a summary assessment, but Net Profit before Tax % and Overhead Absorption % will almost certainly figure in any shortlist.

The table below contains examples of KPIs and associated benchmarks commonly used for the three main dealer departments and the business overall, neatly illustrating how they can be used together to provide an overview of performance and enable analysis of strengths and opportunities (section 1.10 has detailed definitions of all the KPIs listed).

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 KPI	Network Average	Industry Average	Benchmark
Total Dealership			
Net Profit Before Tax %	1.6%	0.9%	2.5%
Overhead Absorption %	68.1%	53.0%	90.0%
Vehicle Sales Department			
New Retail Gross Profit %	8.9%	8.5%	9.0%
Used Retail Gross Profit %	9.7%	9.5%	9.4%
Used: New Ratio	2.4:1	1.5:1	1.5:1
Vehicle Department Expenses as a % of Department Turnover	5.2%	5.1%	5.0%
New and Used Vehicles Sold per Sales Executive	111	143	150
Used Vehicle Stock Turn per annum	6.1	8.0	9.0
Return on Used Vehicle Stock Investment %	65.8%	80.9%	100%
Service Department			
Total Service Labour Gross Profit %	74.0%	75.0%	77.5%
Service Overall Efficiency %	94.0%	86.2%	100%
Total Service Labour Gross Profit %	75.4%	76.6%	76.0%
Service Department Expenses as a % of Department Turnover	36.7%	36.9%	36.0%
Labour Hours per Repair Order - Retail	1.6	1.6	1.7
Service Department Direct Profit %	38.7%	39.7%	40.0%
Parts Department			
Total Parts Sold per UIO (Unit in Operation)	115	130	136
Total Parts Sales Gross Profit %	21.2%	20.4%	23.0%
Parts Department Expenses as a % of Department Turnover	13.6%	11.2%	10.0%
Parts Sold per Retail Job Card £	140	155	165
Total Parts Sales Direct Profit %	11.4%	14.0%	16.0%
Parts Stock Turnaround (Times PA)	9.1	12.8	15.5

1.4 Key performance drivers (KPDs)

A key performance driver (KPD) is a specific action that promotes the improvement of one or more KPIs. Just like a SMART goal, a KPD should be:

- Specific to a process
- Measurable
- Agreed in terms of task and responsibility
- Relevant to the achievement or improvement of a stated KPI
- Timebound

Below is an example of a service department DOC:

Service Department Daily Operating Control										Day	22
										Days remaining	0
Carry Over Gap From Last Month	Month Budget			Month To Date Budget		Month to Date Actual		On Target	Gap		
Hours	Hours	% Mix	Sold Hours	Hours	% Mix	Hours	% Mix		Hours		
10	270	41%	Retail Franchise	270	41%	331	37%	✓			
	0	0%	Retail Other	0	0%	95	11%	✓			
	92	14%	MOT	92	14%	149	17%	✓			
	229	35%	Internal	229	35%	205	23%	✗	24		
	66	10%	Warranty	66	10%	115	13%	✓			
10	657	100%	Total Sold Hours	657	100%	895	100%	✓			
£	£	% Mix	Labour Sales Mix %	£	% Mix	£	% Mix		£		
£897	£21,483	50%	Retail Franchise	£21,483	50%	£26,592	58%	✓			
	£0	0%	Retail Other	£0	0%	£211	0%	✓			
	£7,270	17%	MOT	£7,270	17%	£3,044	7%	✗	£4,226		
	£10,674	25%	Internal	£10,674	25%	£11,034	24%	✓			
	£3,156	7%	Warranty	£3,156	7%	£4,847	11%	✓			
£897	£42,583	100%	Total Labour Sales	£42,583	100%	£45,728	100%	✓			
Budget		KPIs		MTD Budget		MTD Actual					
691	Total Attended Hours	691	770	✓							
691	Total Hours Worked	691	651	✗							
657	Total Hours Sold	657	800	✓							
100%	Utilisation %	100%	85%	✗							
95%	Productivity %	95%	123%	✓							
95%	Overall Efficiency %	95%	104%	✓							
£79.57	Retail recovery Rate	£79.57	£80.34	✓							
£64.81	Overall Recovery Rate	£64.81	£51.09	✗							

1.6 The process of continuous improvement

The concept of continuous improvement is based on the Japanese business philosophy of Kaizen. It encompasses all those actions that continuously improve the outcomes of KPIs in a business, with efficiency, productivity and hence profitability increased by constant enhancement of systems and processes. Although its roots lie in manufacturing, it's equally applicable in automotive dealerships as the principles remain the same.

For example, consider a dealership where the level of paint-protection sales penetration is 35% of new vehicles sold, with the product included in the customer offer as part of the sales process. However, this is low compared to a typical brand average of 55%. Upon investigation, it's discovered that only 60% of customers in this dealership example are also seen by the sales manager and,

even then, in most cases the paint-protection product is not mentioned. If this was to change to the sales manager seeing every customer and promoting paint protection, it could be assumed that the dealership result would improve to the national brand average.

This is a basic example, but it illustrates the continuous-improvement process. If the level of second-facing made no impact on paint-protection sales, then the manager would have to look for another causal factor, such as the salesperson's enthusiasm for the product or how the sales remuneration scheme is structured. In any event, once the manager has determined the root cause of the problem, they can then act to address the issue as will be covered in more detail in the chapter regarding the Service Department.

Continuous improvement is a perpetual process of removing inefficiencies or poor practices to maximise business performance and efficiency. Businesses should strive to adopt this process as it improves competitiveness and profitability.

This is a key principle that applies throughout the business and is referred to as plan, do, check, action (PDCA) as shown in the framework elsewhere.

1.7 Understanding total business financials

Accounting standards differ across international markets. For instance, in the UK, businesses have a highly regulated financial-reporting system. This section focuses on an accounting reporting structure and how it can help dealerships operate consistently within it. Not only is there a common basis of reporting in general, but there is also a very precise form of reporting within the automotive industry itself which accords with these basic accounting standards. The three main accounting statements are:

- The profit and loss account
- The balance sheet
- Funds flow and cash flow

The principles guiding these statements are governed by the Financial Reporting Council. In simple terms, accounts are drawn up on the following assumptions:

- The business is a going concern. For example, stock is valued at the lower of cost or net realisable value, but not as though the business were insolvent or in administration
- The business operates the accruals process i.e., expenses match the revenue they generate (see below for a more detailed explanation). For example, rent may be paid quarterly, but the monthly management accounts show an accrued monthly amount in the expenses on the monthly profit and loss account
- The business operates on the consistency basis, so the accounting approach to the business remains consistent over time. For example, if the general manager's salary is split between departments in one month, then that should be the case consistently i.e., every month
- The business operates on the prudence principle. Examples of this are that stock is not overvalued, or that a provision is made against bad debts. In other words, the business takes a cautious view of both revenue and expenses

The principle of accruals is fundamental to the method of accounting. It is an accounting concept that requires transactions to be recorded in the accounting period in which they occur, regardless of when the associated cash flows for those transactions are received or paid. The idea behind the accruals principle is to match net sales against their associated expenses when a transaction (such as a sale) occurs, rather than when the actual payment for the transaction is received.

Accounting information produced for external use falls under the heading of financial accounting. This includes statements that must be submitted to any statutory bodies annually, for example in the UK, Companies House. These are externally audited and must adhere to standard accounting principles and conventions. Management accounts are used internally in the day-to-day running of a business to assist with performance measurement, strategic planning and goal setting. A clear and defined structure for these accounts has become established within the retail-vehicle sector, as shown in the rest of this section.

1.7.1 The profit and loss account

The profit and loss account shows the difference between the flow of revenue and the flow of cost of sales and expenses over a defined period. In the case of management accounts, these can be for a week, a month, a quarter, a year, or any other period. In practice, nearly all companies produce monthly and annual management accounts, and all produce annual financial accounts.

The format of a profit and loss account is shown below:

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The Profit and Loss Account	
Invoiced Sales (cash or debtors)	
less	Cost of Sales (cash or creditors)
=	Gross Profit
less	Expenses (including depreciation and stock write down)
=	Net Profit Before Interest
less	Interest
=	Net Profit Before Tax
less	Tax
=	Net Profit After Tax
less	Dividends Payable
=	Profit for Re-Investment

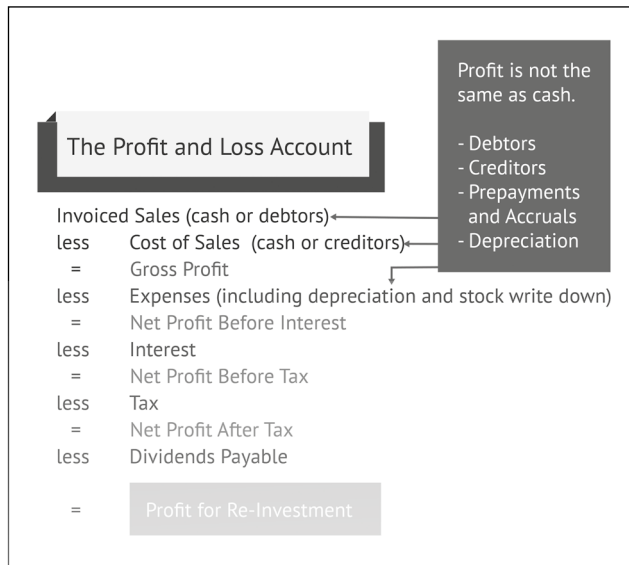
Note that:

- All sales or turnover figures are shown net of discount and VAT. This is an important point to note. All KPIs that include the terms sales, turnover and net sales are referring to sales, turnover and net sales after any discount given. Therefore, a discount is a reduction of the gross sales value. VAT is also excluded from these figures. Management accounts and composite reports therefore express expenses, costs, gross profits, direct profits and net profits as a percentage of net sales. Note that gross sales are before any discount is given
- Gross Profit is sales minus the cost of units or items sold. It can be expressed as a £ figure or as a percentage of the turnover
- The key figure to look for is the KPI of Net Profit before Tax (section 1.10.1). This represents the business' total revenue after all business expenses and costs of sale have been deducted

It's also important to realise that profit is not simply a reward for the shareholders. Profit is needed to fund growth in the business, either in fixed assets or working capital. Neither is profit the same as cash, for the following reasons:

- Some sales are sales on credit (debtors) and therefore don't immediately bring cash into the business
- Many purchases of services are also on account and therefore aren't immediate cash outflows (creditors)
- Depreciation is a non-cash expense, as are payments in advance or arrears for goods and services (prepayments and accruals)
- There are also many other transactions that affect cash but not profit, and vice versa

The table below shows where some of the differences between profit and cash arise. Understanding this is critical since a business may be profitable, but without cash it cannot continue as a viable concern. Therefore, companies produce separate cash-flow statements.



1.7.2 The balance sheet

The balance sheet differs from the profit and loss account in one important aspect. It's a statement of the company's position at a point in time, usually the fiscal year end, although balance sheets can be produced monthly within management accounts. Unlike the flows of sales and expenses noted in the profit and loss account, the balance sheet is not the difference between two flows over a period but instead consists of assets and liabilities, and it always balances.

In simple terms, assets are what the company owns, liabilities are what it owes to external parties.

- Assets are divided into fixed assets and current assets. Fixed assets are those required to run the company (e.g., property, plant and equipment). Current assets are items for sale or consumption.

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