

Wipe the Windows, Check the Oil, Ten Dollar Gas

My apologies to The Allman Brothers Band, but rising energy prices, a credit crunch, and sluggish consumer spending can have a negative effect on our business environment. The good news is that taking a proactive approach toward the aforementioned factors can have a positive impact on your company's performance outlook during difficult economic times. I recommend that you take the following steps to prepare your company to meet any challenges that may lie ahead.



**PROFESSIONAL
OPINION**

James V. Mungillo, CPA

1. Evaluate your Company's Situation (Wipe the Windows)

If your windshield is dirty, it is more difficult to see what is in front of you. Like a dirty windshield, not having a clear picture of where your business stands financially can inhibit making correct operating decisions. Businesses fail simply because their owners and managers are unprepared for crises. They either cannot see the critical factors that precede a crisis, or they detour around the critical factors because they do not want to deal with them. In some cases, they do not have the time to properly address them, or they see the critical factors but focus on solutions in the wrong areas.

Bad or inaccurate information can sometimes be worse than no information at all. For example, cash in the bank is not always the best gauge of business performance as it does not take into account a multitude of other economic factors. Besides the traditional financial statements, a host of liquidity, profitability, debt, operating, performance and cash flow ratio indicators should be available for you to see quantitatively what's on your windshield. A few more recognized gauges include: the current ratio; profit margin analysis; return on equity; debt to worth; debt coverage; and free cash flow. EBITDA, or earnings before interest, taxes, depreciation and amortization, is another often used calculation to determine a company's financial direction. This analysis should cover multiple years and take into account non-financial fac-

tors such as industry trends, personnel changes, and interest rates.

2. Check your Cash Flow (Check the Oil)

Much like an automobile needs oil, your business needs a steady flow of cash to operate. Your employees expect to be paid, and vendors may not tolerate lack of payment for purchases for too long. Do your homework by evaluating your

cash flow needs via projections using a worst-case scenario or conservative approach. (For example, project sales at lower levels than truly expected; increase your cost of sales so as to cut your projected profit margins; and adjust selling, general and administrative expenses for potential expense increases in auto, freight, travel, and utility costs.)

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A simple cash flow analysis can be created by starting with your existing cash, adding in your expected cash collections from cash sales or accounts receivable, and then subtracting cash outlays for reductions in accounts payables, cash payments for payroll, selling, general and administrative expenses and monthly loan and interest payments. You should also factor in other available sources of cash such as lines of credit and capital infusions from the owners during months of negative cash flow. Obviously, negative cash should only be cyclical and/or short-term based on seasonal sales cycles. Long-term negative cash flow is an indication of potentially more serious problems and is a sure sign that change is needed.

You should also understand your monthly fixed costs: those costs that remain constant regardless of the sales

level achieved. A break-even sales analysis takes into account these fixed costs and will assist you in determining a sales level necessary to cover these fixed expenses as well as the variable expenses to generate that sales level.

3. Look Ahead and be Ready to Change (Ten Dollar Gas)

My earliest recollection of the price of gas goes back to my childhood trips to the gas station with my father. A dollar entitled us to three gallons of gasoline. Today, a dollar gets you roughly a quart of gasoline. The majority of this price increase has occurred over the last 10 years. When it looks like change is coming at a fever pace, planning ahead is essential. Business owners and managers are likely the best yardsticks for evaluating a company's future performance. Managing a company's financial operations, now more than ever, can be more important than managing the day to day operating activities. Know where you stand, implement regular reviews of key financial indicators and act upon them.

The most important advice I can give is this: Be ready to change. Do not fear change. Do not sidestep critical issues in the hope that they will go away. Smart business people lead with their heads more than their hearts. Difficult or unpleasant decisions will not go away simply because you choose not to act on them. Do not spend what you do not have. Make the necessary changes in the levels of personnel, operating expenses, asset holdings and purchases, and debt levels. Do business with people that pay you, collect what is owed to you and take advantage of available discounts. Err on the side of conservatism; and most of all, make good, sound business decisions. If you fail to act, you are really acting to fail!

Remember, business failures happen very slowly over time, and then all at once.

If you feel unsure of the decisions to make, consult a professional for assistance. It will be money well spent!

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