Ask SCORE

I'm a retired sales and marketing guy who's recently purchased a local convenience store. What are some of the key numbers I should be monitoring to successfully manage the business' finances?

Anyone who longs for the "good old days" probably doesn't own a small business. Given the variety of powerful, easy-to-use accounting software products available today, it's difficult to imagine wanting to keep records and prepare financial statements by hand.

But while technology has eliminated the need for stubby pencils and green eyeshades, it's still up to the small business owners to analyze and understand the meaning of their financials in order to make wise decisions.

While there's no hard-and-fast rule for reviewing financial data, most experts recommend a minimum of monthly or quarterly evaluations. Otherwise, you risk spotting serious problems too late to take corrective action.

Cash flow is a key indicator to watch. This is the revenue coming into your business balanced against expenses (rent, payroll, supplies, etc.). Projecting cash flow into the future will help alert you to potential bottlenecks in meeting payment obligations, and whether changes in your collection strategy or operating budget are warranted.

Several financial ratios can also help small business owners gauge the health and progress of their enterprise. Because these ratios fluctuate over time, tracking them will help you better spot trends that could evolve into opportunities or problems.

Liquidity ratios measure the firm's ability to meet short-term commitments from its liquid assets. The current ratio (current assets/current liabilities) is a simple measure of a firm's ability to meet short-term obligations. Similarly, the quick ratio (current assets minus inventory/current liabilities) measures the firm's ability to meet short-term obligations from its most liquid assets. The ideal average for both varies from one industry to another.

Leverage ratios indicate the company's ability to meet both long- and short-term obligations, making them particularly important to bankers and investors. The most frequently used indicator is the debt ratio (total debt/total assets). Generally, lenders want this ratio to be as low as possible.

Profitability ratios measure how well a company earns a net return on sales or investments. Gross profit (gross profits/net sales) measures the margin on sales, essentially the overall effectiveness of the business. Net profitability (net income/net sales) shows the effectiveness of management in controlling costs.

Then there are activity ratios, which show how well a company uses its assets to generate sales. Small businesses that manufacture or sell products should monitor inventory turnover (cost of goods sold/average inventory), while businesses of all types should watch their average collection period (average accounts receivable/average credit sales per day) to determine if they are being paid promptly.

This column is brought to you by the Merrimack Valley Chapter of SCORE, with nearly 70 current and former business executives available to provide free, confidential, one-on-one business mentoring and training workshops for area businesses. Call 603-666-7561 or visit merrimackvalley.score.org for information on mentoring, upcoming workshops and volunteer opportunities. SCORE is a national, non-profit organization and a resource partner of the U. S. Small Business Administration.