CFO Insight – Fact Sheet

Taking Control of Profit

'Profit' is what's left over after you've paid all your expenses. The important thing to note is that profit is '*what's left over*'. PROFIT IS A RESIDUAL. It is a consequence of what happens in and to your business. Some of these things are within your control and some of them are outside your control. If you're going to have any effect on your profit, you have to focus on those things over which you have control.

As it turns out there are **four specific factors** that determine profit and over which you have some degree of control. These are:

1. The **PRICE** you charge for the products and/or services you sell.
2. The **QUANTITY** (or volume) of products or services you sell.
3. The costs you incur directly in producing or buying the products and services you sell. These are referred to as **VARIABLE COSTS** because they increase or decrease as your sales increase or decrease.
4. The costs you incur whether you make any sales or not. These are called **FIXED COSTS** because they don't change with changes in sales volume, at least not on a day-to-day basis.

CFO Insight offers a profit improvement potential analysis service that works by running '**what if**' scenarios on the business' figures to demonstrate how significant improvements to profitability can come about from just small changes in these four factors. However, you can do it yourself.

These start by using your current figures as base and estimating what would happen with a small increase or decrease. In the table below let's assume the current figures are in the BASE column and make a 5% alteration to give the figure in the RESULT column.

In this example, a **modest 5% improvement** in each factor (without any consequential unfavourable impact on any of the other three) would more than double your profit from $1,000 to $2,190. This is a **119% improvement** in profit and from only a 5% improvement in each of the factors that affect profit.

It is evident that a relatively small % change in each of the four factors has a staggering effect on the resultant profit. And of course the reverse is also true. If you discount your price, allow your sales volume to fall, fail to control your fixed costs and let your variable costs get away from you, even by small amounts, you can end by destroying a profitable business.

	BASE	**CHANGE**	**RESULT**
Price	$100	5% increase	$105
Sales Volume – units	100	5% increase	105
SALES	$10,000		$11,025
Less VARIABLE COSTS ($60 each)	$6,000	5% decrease ($57 each)	$5,985
Gross Profit	$4,000		$5,040
Less FIXED COSTS	$3,000	5% decrease	$2,850
NET PROFIT	$1,000		$2,190

Obviously to make the increases happen you need to review your operations in the areas that affect the figures – cost cutting, process improvement, more active marketing and so on. But the results can be well worth the effort and cost of implementation.

*If you would like further help on how you can take control of your profits, or to simply discuss issues you have about your business, please call **Philip Barnes**, Director, CFO Insight on **0405 800 767**.*

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