



QUARTERLY FINANCIAL REPORT: How Do You Stack Up?

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Inc. Magazine | November 2008

Have you ever wanted to peek at your rivals' books? Now you can. We have compiled detailed financial data—from margins to debt levels to receivables—on companies in a dozen industries. Turn the page, and see how your business compares.

You are scanning a spreadsheet of your company's financial performance, and it all looks pretty good. Gross margins are stable, net profits are up, and your customers are paying you in 45 days, down from 50 last year. But how are you doing compared with others in your industry? What if your rivals' margins are even stronger? What if their customers pay in just 40 days? Suddenly, your situation doesn't look so rosy. "Knowing your own number is only half the story," says Brian Hamilton, founder and CEO of Sageworks, a Raleigh, North Carolina, company that makes software for bankers and accountants and maintains a trove of data about thousands of private companies. "When you look at how you compare to your papers, you can see where you're strong and what you need to work on."

The problem is that it's nearly impossible to learn where your rivals stand, especially if you compete against other small, privately held firms. On the page that follows, *Inc.* seeks to remedy the situation. We asked Sageworks to dig into its database and come up with detailed financial information for companies in 12 industries. Then, we asked a number of seasoned CFOs to provide insight into which metrics matter for which industries and why. Are you as profitable as you could be? Are you generating as much cash as you should? Turn the page, and find out. Of course, these data are no substitute for hiring an experienced CFO of your own. But they may help you answer the question: Are your competitors doing better than you? — *Hannah Clark Steiman*

Regardless of what industry you're in, if you ever plan to seek a loan, pay close attention to your debt to equity ratio, says Michael Foos, a partner at B2BCFO, a company that places temporary financial executives. Particularly in today's tough credit market, it's best to keep the number under 2 if you want bankers to see you as a good candidate. You can manage this ratio by putting more equity in the business. For example, if you have loaned money to your company, turning that into an equity investment could dramatically improve your numbers.

INDUSTRY FOCUS: FOOD SERVICES

For food businesses, managing inventory is crucial. For those that make frozen foods, 12 days is a good target says Wayne Lorgus, a partner at B2BCFO, whereas restaurants want to keep inventory on hand for only a couple of days. But Lorgus notes that rising transportation costs are forcing some companies to order supplies in larger quantities to get a discount. The bottom line: If your inventory is higher than the industry median, make sure you have a valid reason for it.

The current ratio measures all assets including inventory. The quick ratio, by contrast, measures only cash and accounts receivable. As long as both ratios are higher than 1, you have enough cash to pay your bills. Your CFO will be happier if they top 12. “Look at your industry,” says Foos of B2BCFO. “If you’re distinctly off, you need to understand why.” Watch these ratios, and take notice if they worsen over time, because that means your sales aren’t keeping up with your bills.

For many CFOs, debt can never be too low. “I love less than 1,” says Mike Eitler, a CFO partner with Tatum, a consulting and staffing firm. “I think it really unencumbers management to focus on providing better products.” But a debt to equity ratio above 2 isn’t necessarily cause for concern –it simply means the company has decided to use debt rather than equity financing, which is common in construction and other capital-intensive industries. Companies need to monitor the number, however. A higher ratio forces managers to focus intently on cash flow and paying down debt, to the exclusion of business-building activities.

In most industries, if it takes your customers an average of 44 days to pay bills, you’re doing pretty well, says Eitler. “You’re out of control if you go over 60.” But he says the trend is more important than the absolute number. If the number is rising, that means you have less cash coming in, and you may be digging into retained earnings or borrowing money to pay bills.

Your shareholders will compare your return on equity to the returns they could get from other investments. If they can make more money by investing in low-risk Treasury bonds, they may go ahead and do so. “If we have ROE that’s less than our cost of capital, then we’re destroying value,” says Geoffrey Huggins, senior vice president and corporate controller at Charles Schwab. In general, most companies want a return on equity at least 12 percent, but financial companies should shoot for 15 percent to 20 percent or even more, Huggins says.

INDUSTRY FOCUS: HEALTH CARE

Monitoring receivables is key for health care firms. Some providers, such as dentists or chiropractors, deal in cash, which brings down the industry media. But others, such as labs, hospitals, and outpatient clinics, can see receivables reach 80 days or more, because of slow insurance payments. When that happens, providers need to find out why; it may be, for example, a simple problem with the way the practice is billing Medicare.

INDUSTRY FOCUS: LOGISTICS

Logistics firms sometimes have a low number for accounts payable, partly because their fuel bills are due within seven days, says Sheri A. Pawlik, a partner with B2BCFO. So although 20 looks good compared with other industries, don’t get too cocky—it’s the overall trend that counts. When a company in any industry starts to deteriorate, it often shows in a rising number for AP days. Says Pawlik: “They’re trying to finance everything by not paying their suppliers as quickly as they otherwise would.”

If you are investing in new equipment, your EBITDA margin should be four or five percentage points higher than your net profit margin, says Neal Restivo, a CFO partner at Tatum. Because the average difference between the two metrics here is closer to 3 percent, that means businesses haven’t been depreciating assets—and are probably relying on old machines. That may reflect rising costs and the softening economy.

INDUSTRY FOCUS: PROFESSIONAL SERVICES

CFOs at professional services firms expect high margins—at least 67 percent—because the cost of sales is low; basically, the only thing that goes into the product is labor. “If your gross margins go below 50 percent, think about changing your business model,” says Richard Block, a CFO partner with Tatum. Maybe, for example your employees are collecting paychecks even when they are not working on a project. Instead, Block says, think about classifying them as contractors and paying them only when they work.

Most companies hold on to their cash as long as they can; if a bill is due in 30 days, that’s when they will pay, and not a moment sooner. Some businesses believe that paying earlier will endear them to their creditors (and professional services firms often have enough cash on hand to do just that). But Terry Eve, a partner with B2BCFO, says companies should always wait as long as possible before sending cash out the door: “At the end of the day, nobody gives you bad marks as long as you pay to terms.”

INDUSTRY FOCUS: REAL ESTATE

For real estate firms, CFOs like to see a gross margin of 93 percent to 95 percent and an EBITDA margin of around 25 percent, says John M. Blackstock, a partner with B2BCFO. The lower averages here, he says, reflect the real estate downturn. But profits aren’t the beginning and end of the story; real estate firms must also pay close attention to debt. The interest coverage and debt to equity ratios determine how much of your profits go to pay down debt and how much return to you.

INDUSTRY FOCUS: RETAIL

Because retail is such a risky business, equity investors generally stay away. As a result, retailers often have a lot of debt which they must manage very carefully. The interest coverage ratio should be 6 or higher, with 8 being a healthier target,” says Geoff Holczer, a Tatum CFO who has served as a financial executive at several large retailers. You may be in trouble if your company’s debt to equity ratio rises above 4. Ideally, for growing companies it should be lower than 1.5. “The best answer is, it should be 0,” says Holczer.

For retailers, the current ratio—which measures all assets, including inventory—often looks much better than the quick ratio, says Holczer. In general, for retailers, both should be higher than 1, except in certain seasons; as inventory builds before the holiday season, for example, payables will increase faster than sales, and the quick ratio will drop.

Banks are more likely to lend to a company with a high interest coverage ratio—more than 6—because it measures how easily the business can repay its debts. But companies that have recurring revenue, such as some software publishers, often can borrow more, even with a low number for interest coverage, says Roger Scadron, managing director at FTI consulting. “If you can find a recurring revenue business model, that’s where you want to be,” says Scadron. “It sure is better than waking up every day and starting with zero.”

Return on assets is a key measure for wholesalers that have large investments in equipment. Return on equity is more relevant for those that don’t. But companies shouldn’t focus exclusively on those numbers; rather, they should focus on all the metrics that contribute to them. Gross margin and inventory days are two of the key metrics for wholesalers,” says Dean Gardner, a CFO partner with Tatum. If your gross margin is 30 percent or higher and inventory is under 45 days, he says, “ROE and ROA should take care of themselves.”