

# How to milk the business cow

Written by John Kelly



If you are the owner of a small business, one of your most important business strategies is how to milk the business cow.

In business profit is the name of the business game. If you do not make a profit your long term sustainable future is limited. Why? Let us look at the analogy of the business cow. The business cow produces milk which is the profit of the business. There has to be enough milk to go round to allow the business owner to:

1. pay the tax man
2. meet loan commitments
3. pay the business owner a living
4. pay for any changes that must be made to the business to keep it up to date
5. Fund future growth and keep feeding the cow

If there is not enough milk produced by the business then you will always be borrowing money to expand or replace assets. The more you have to pay back to the bank the less there is for you the owner to pay yourself well and therefore to provide for your long term future – your retirement.

For the owner of a small business, it is not usually their expectation that the business when sold, will provide totally for their retirement. The smart ones put aside money over a long period of time to ensure that these investments together with the sale of their business will give them enough to retire on.

How much is enough? This depends on your circumstances and your financial needs. If you wanted to live on a \$1000 per week after tax and keep your assets pretty much intact for the remainder of your life, you would need around \$1.2 - 1.4M, over and above your house.

Where are you now in relation to these figures? Consider the following example of David. David sought the advice of Kelly & Co to establish where he was in relation to where he wanted to be as regards the value of his business and his investment assets. The facts as they were presented by David were as follows:

David was (53), the owner/operator of a successful business providing support services to the building and construction industry. David had started thinking about finishing work and believed all it would take is not getting out of bed to go to work. Until he spoke to us, David was looking forward to



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retirement. He was planning to sell his business to fund part of his retirement. He didn't realise how the shortfall in his business value affected his future lifestyle. Based on his retirement plans, David's adviser had estimated he would need \$1.25 million in retirement assets at aged 60. His projected income earning retirement assets were \$575,000. His asset shortfall of \$675,000 far exceeds the current value of his business.

If David did nothing he would face:

- o Accepting a lower standard of living at retirement
- o Continuing to work well past his retirement date

David's FIRST STEP was to complete a Business Value Gap analysis. This identified:

- o his value needed at sale
- o what the business was actually worth
- o the difference between value needed and actual value is called the 'value gap'
- o the profit target required to achieve the value he wanted

One important fact David learned from Kelly & Co is the direct link between the amount of milk produced by the business cow and how this affects the value of the business.

Essentially the only strategy open to David was to produce more milk. How could he do this? He needed to identify those items that impacted on the value of his business and then build a business growth strategy. The drivers of value in an SME are:

1. is your business reliant on you
2. do you have quality clients/customers
3. is your business innovative and different
4. do you benchmark your business performance
5. do you have loyal and committed staff
6. do you have excellent business systems
7. do you have an exit strategy a "Succession Plan"

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## Conclusion:

Your business is a cash cow and it must be looked after.

On your business journey you should be using some of the milk to invest outside of your business.

You need to establish how much money you need to retire with and how this will be reached. If you need your business to fill the “gap” between what you have now and what you need for your future, then you have to devise strategies to increase the value of your business.

The only way to increase the value of your business is to make more profits.

Kelly & Co specialises in growth and transition planning. Please phone John on (03) 466 5062 for assistance. Visit our website [www.kelly.co.nz](http://www.kelly.co.nz)



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