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Best Practices in F&B Financial Reporting-Part III

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Continuing the discussion started in my last article, which focused on F&B companies needing strong balance sheets to further growth, this article will focus on best practices in income statements, operations, and ratios.

Budgeting

Budgeting or forecasting is extremely important for F&B companies of all sizes. Many companies use top down or bottom up approaches, but regardless, it is unacceptable when a company says it can't do a budget. It's like saying any old road will get me there.

Best practices dictate a customer-by-customer and product-by-product approach to projected sales for the coming year. By the way, next year's budget should be completed in the fourth quarter of the current year. The sales projection should take into consideration new product sales and new customer acquisitions, and should correlate with each salesperson's goals and initiatives. Budgets cannot be created in a vacuum, and the projected income statement should correlate with a projected balance sheet and cash flow statement. Major errors are often made in the absence of this three-way integrated model.

Many companies will throw out the budget when projected results differ significantly from actual results. To avoid this problem, combine actual results with projected results for the remainder of the year to get a better idea of where you might wind up at year-end. A best practice is a six-column income statement where the first three columns address monthly amounts as follows: month actual, month budgeted, month prior year. The next three columns address year-to-date totals as follows: actual year-to-date, budgeted year-to-date, and actual prior year year-to-date. Inserting percentages of sales or other metrics such as dollars per pound or dollars per unit is also very helpful in identifying problems.

The final step is to critically evaluate whether the budgeted amounts were correctly forecasted and ways to improve projections in the future. And then you start the process all over again.

Management Discussion and Analysis (MDA)

While public companies always have a management discussion and analysis in their financial documents, private companies rarely do. Properly memorializing what really happened in the past period and what's ahead for the future is invaluable information to shareholders and investors. It explains the "whys" behind the numbers, good or bad. It explains how management reacted to the issues and what processes are in place to ensure mishaps don't occur in the future. It can also address economic factors or competitive factors or regulatory issues that may have affected the company during the period reported on. This document should become part of all financial data published by the company.

Ratios and Benchmarks

While there are specific ratios and benchmarks for distributors or restaurants and others, there are some universal ratios and benchmarks which are important to track. The first is a liquidity ratio (the current ratio) where you divide current assets (assets turning into cash within one year, generally) by current liabilities (liabilities to be paid within one year). A one-to-one ratio means you have just enough assets to cover your liabilities. Anything less than 1:1 is dangerous.

Another critical ratio is debt-to-equity, which is all of your liabilities divided by your net worth (equity) in your company. Anything more than 3:1 signals too much leverage and could cause you problems with lenders.

Everyone knows about EBITDA (your bottom line with add-backs for interest, taxes, depreciation, and amortization) and your EBITDA percentage as it relates to sales. With bottom lines so thin, this benchmark is one of the most important ones to monitor. In the next article I will address strategic planning.

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I am the national leader of Marcum's Food and Beverage Services group. I've been an entrepreneurial leader in accounting for over 40 years, and am a frequent lecturer and published author on various financial and business topics. My expert advice has appeared in both nationa...