YOUR Knowledge

Preparing for the rollercoaster ride

Standards and Poors has downgraded America's AAA credit rating, local and international markets are volatile and easily spooked, picking changes in interest rates is more akin to crystal ball gazing, the carbon tax is coming, consumer sentiment remains tight and no one is feeling particularly confident. Welcome to the 2011/2012 financial year.

Over the next 12 months business will be working with a range of domestic and external influences that will cause uncertainty. But these swings can be a benefit as well as a headache – but only for strategically sound businesses.

Most SMEs are well downstream from major economic triggers. We don't cause the problems but are affected because of what is happening to larger businesses, the economy, and consumers. Some industries are more impacted than others.

Expecting business conditions to be 'more of the same' over the next 12 months is wishful thinking. If your business strategy is simply to turn up, work hard, and expect business to come to you then you are likely to be disappointed. If you have not already, it's time to do something different. When business gets tougher, 'me too' businesses come under pressure. A 'me too' business is one that simply replicates what everyone else in their industry or sector does. You work on the basis that there is a consistent and proven formula and if you follow the formula everything should work out. Sounds ok in theory (and says a lot about human nature) however the problem is that you are doing nothing to differentiate yourself in your market. This lack of differentiation may leave your customers with no compelling reason to continue doing business with you.

Business, and in particular small business, needs to be more strategic. The objective needs to be more than carving out some market share but to create a sustainable business. This is where your business strategy comes in. Your strategy should set the direction for your business and allow you to carve out a sustainable position in your market. In a buoyant market you can survive without a strong business strategy; there is plenty of business for everyone. Turn up, work hard, and you will pick up some market share. The challenge in the good times is generally supply rather than demand.

In a volatile market, demand can be patchy and in some cases depressed. Everyone is chasing business and if you don't have a clear business strategy then it is likely that you are trying to win business by chance or competing on price. Most SMEs are not equipped to compete on price. You don't have the capital reserves or the economies of scale to compress your profit margins. Go too far and you can trade yourself out of business. *Continued over the page...*

Developing a business strategy takes time and hard work. You need to understand your industry sector, your market, where the opportunities lie, and how you can differentiate your position in that market. It's not easy but get it right and it will pay big dividends. As a starting point you need to identify what your current business strategy is. You should be able to clearly articulate it and write it down (in your head is not good enough). If you don't have one then accept reality and start working on one. Your strategy should flow into your business plan and then be reflected in your operating and cash flow budget for the year. Typically, your business strategy will contemplate your end game – be it a sale of the business or some other exit event.

Good businesses always have a clear strategy in place. For the coming year it will be more important than ever; it will separate the successful from the strugglers.

Talk to us today about how we can help you refine and improve your business strategy.

5 tips to differentiate your business

- **Focus on the customer experience**. What's it really like dealing with your business? Do a blind test and see whether your business and your team really want customers and sales. For most businesses, you're not delivering a product/ service, your delivering an experience.
- **What do your customers really want** and can you give it to them and still make a profit? Starbucks closed 61 stores in Australia by 2008 (73% of their stores). They misunderstood the sophistication of Australia's coffee market and no amount of advertising was going to make us change our barista. *Continued over the page...*

YOUR Knowledge

Don't pay more tax than you need to

If you are finalising your end of financial year accounts and calculating your tax position, keep in mind that there are still options available to save you tax. One of these options impacts on the valuation of your trading stock and if stock is a material asset in your business, you should most certainly consider it. This option provides you with different valuation methods that can be applied to your trading stock.

The majority of businesses value their trading stock at cost and in many cases this is the right valuation approach. However the Tax Act gives you the choice of valuing your stock at the lower of cost, market, or replacement value.

Your trading stock is an asset that is recorded on your balance sheet. In most cases it should be tax neutral to you. The cost of purchasing stock is expensed in your profit and loss account and is offset by the value of the stock asset, until you sell it. So, while the amount of stock you are carrying will impact on your cash position, because you have your funds tied up in it, there is no direct impact on your profits or taxable income until you sell that stock. However, if at June 30 some of your stock is worth less than its cost price, you have the option to value it at the lower figure and take the tax write off now, rather than wait until the stock is sold. This reduction in your stock value will produce a tax saving for you.

There are a range of reasons why stock values may be less now than at the time you purchased the stock. For example, stock becomes out of date, obsolete, damaged or changes in demand mean that the stock can only be realised at a discounted price. Other than when you sell your stock, your tax return gives you a once a year opportunity to adjust your stock values and realise on any losses.

You don't have to use the same valuation method for all of your stock as the trading stock valuation options can be taken on an item by item basis. So, you can elect to use different methods for different stock items. In many cases cost price will be the appropriate valuation method. You would normally consider using market value or replacement value for stock items only where there has been a fall in value. It will be important to have sufficient documentation to both record what action you have taken and also to justify the value you arrived at. If you are subject to a tax audit you will need to be able to substantiate the value being used. This means having your stock count and also the itemised values for each stock item. Where the value being used is not cost price there should be a clear basis for the amount used.

Where you have experienced a fall in stock values it normally makes sense to take the tax write off now. We all know that cash is king at the moment and the tax saving will help to cushion some of the loss.

Got a question? Talk to us today about how we can make a difference to your businesses.

Tips to differentiate your business *continued*

- **Solve the problem**. What is it that your business does for your customers? The more you can solve the problems they face and make life easier, the more likely it is that customers will choose you over your competition. It might be as simple as refining how customers choose and order your product, access to information that is valuable (think of the freight companies who offer freight tracking and schedules of a customer's history) through to product development (online banking didn't always exist).
- **Know your product**. Do all of your staff know your product or service and do they know what to say about it? The business might seem simple to you but your staff might not naturally realise what needs to be done or said. Inexperienced or poorly trained staff are a huge turn off to all but the keenest customers.
- **Not everyone wants to be your friend**. For many years marketers told you to develop a close relationship with your clients. As a result, everyone wanted you on their database primarily to market to you (almost zero value to your customer). There is no question that there is a value to having a tangible customer base. But realise that your customers are looking for different relationships with different businesses. Understand what it is they want from you and develop the relationship from there. If you make contact give them value - don't just talk at them about your product.

Quote of the month

"Price is what you pay. Value is what you get." *Warren Buffett*

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