Entrepreneurs

How To Keep Tabs On Any Business

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Look beyond your income statement for more meaningful metrics.

There is always less room for error when the economy goes south.

But benchmarking your business means a lot more than tracking revenues, gross margins and debt ratios. To truly a get a handle on your company's health, you have to look beyond income statements and balance sheets.

Every industry has its own peculiar metrics. (What the restaurateur might track is different than what the contract manufacturer might.) But there are plenty of commonalities, too: The importance of things like capacity utilization, process control, sales cycles and repeat customers apply no matter what business you're in.

Take manufacturing, for example. On the surface, making widgets is one of the easiest business models to grasp. But squeezing out a few extra dollars of profit takes more than meets the eye, says David Pittaway, senior managing director of Castle Harlan, a Manhattan-based private equity firm.

For extra perspective, Pittaway and company lean on a metric called the "cumulative first-pass yield." Don't let the name scare you--this concept is elegant and powerful, and the calculation is straight forward. Simply divide the cumulative number of units made correctly the first time by the number of units put through the process; plot the results on a trailing, 12-month basis.

The beauty of this ratio is that it sheds light on both productivity and process control. An increasing percentage means your manufacturing process is improving. Measuring on a 12-month trailing basis eliminates blips associated with suddenly different order sizes.

That's an operational metric. How about one that speaks more to strategy? Matthew Growney, founder of Isabella Products, a consumer electronics developer in Concord, Mass., looks at contract engineering and manufacturing capacity within the U.S. This represents the amount of resources currently un-deployed yet available to crank out new products.

Going into the first quarter of 2009, the number stands at 50%--meaning that there are plenty of idle plants out there. Growney figures that small, nimble players like him can probably negotiate good deals from top-tier manufacturers who need to put their people and equipment to work. (In other words, entrepreneurs, strike while the iron is hot.)

Now think about professional services. Like any business, running a law firm or consultancy is all about getting the most out of each hour slogged. But there are a few ways of measuring capacity utilization, and they each tell you something slightly different, points out **Gene Marks, founder of the The Marks Group, a small business consultancy (and Forbes.com columnist).**

For example, if you want a better bead on which employees are carrying their weight, you could measure billable time per employee (total hours charged to a client divided by total hours spent serving them), or total expenses per head (salary, benefits and all non-billable expenses).

Maybe problems lurk in the job-estimating process, dooming longer-term projects from the start. To check it out, divide actual time incurred on a project by the initial estimated time. This ratio will give you a sense for how reliable your estimating process is--and, in turn, how to price your services. If quotes are too high, you'll lose work; too low, and you'll lose money.

Technology is traditionally considered a growth business, and that often means an obsession with the top line. The problem is that revenues don't tell you a whole lot beyond the general (backward-looking) direction of overall demand. What you're really after is improving the sales process itself.

One place to start is the sales cycle--defined as the time between your first sales meeting with a client and the close of the deal. Generally speaking, the shorter the sales cycle, the better (though some longer cycles may yield larger average purchase orders). Longer sales cycles might be a sign of a weak sales force, wrong customer mix or an unloved product.

Successful restaurateurs also need deeper perspective than their income statements will ever convey, notes Bryan Pearce, Northeast strategic growth markets leader at Ernst & Young. Two useful metrics here are the average ticket per customer and the number of customers. Just knowing how much your customers spend on average doesn't tell you enough; you also need to know how often you turn those tables.

The key is using these metrics in concert. Fat cats who rack up big tabs but stay for three hours may not be as profitable as more modest customers who chow down and keep moving. Depending on what the data say, you can then play around with menu items and pricing to maximize throughput and profitability. If ticket prices and volume are declining, try expanding take-out options to get more out of your idle kitchen, says Pearce.

If you're not tracking customer satisfaction, start now, says Jason Gries, chief executive of Industriaplex, a logistics firm in Apharetta, Ga. Sourcing suppliers, delivering orders and supplying flex conveyors and pallet jacks isn't exactly sexy stuff--which is why it helps when satisfied customers do your marketing for you.

Gries employs a little trick he learned as an executive at General Electric (nyse: GE - news - people), the king of managing-by-metrics. It's called the "net promoter score," and it's defined as the percentage of "promoters" minus the percentage of "detractors." A promoter is a customer who scores your company's performance, on a one to 10 scale, between 9 and 10, while a detractor gives it between zero and three. Ask customers to rate your performance on multiple levels--on-time delivery, cost-savings, etc. Total up the scores and track them over time. You'll know soon enough how things are going.

Clearly, better metrics can help entrepreneurs understand what drives profits and sustainability. In a downturn, though, one metric matters above all: how much cash you have in the bank.

Says Ernst & Young's Pearce: "The public markets may not return for 12 to 24 months, so you need to understand if you have enough cash to stay alive until then." (For more on smart cash management, click here.)