

The Profit and Loss Statement



OTHERWISE KNOWN AS: the Income Statement or Earnings Report.

PERIOD: like a movie, it measures financial transactions over a period of time, such as a month, quarter or year.

FORMULA: Profit = Sales – Costs

IMPORTANT TO UNDERSTAND:

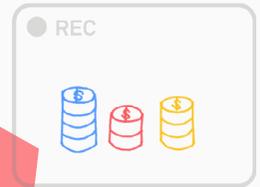
- Costs and sales are recorded when invoices are received or sent, not when the cash transfers occur.
- Large long-term asset purchases have their costs spread over time in line with their decrease in value using accounting mechanisms called depreciation and amortisation.

SOME OF THE THINGS IT TELLS YOU:

- Whether you will make or lose money.
- How efficient you are at making money using your business model.
- How you compare to other similar businesses.
- How you could increase your profits, for example, by cutting costs, raising prices or increasing sales volumes.
- What your fixed versus variable costs are and how to manage both in terms of risk, profitability and growth.
- Whether you spend too much per sale.
- Whether you spend too much on fixed costs.
- How you could adapt your business model.
- The effect of market entry timing.
- How the business will grow.
- Whether critical financial issues exist.
- How much tax you will have to pay profit in the period.

Example Profit and Loss Statement

FORECAST FLOWERS - MONTH 1



The direct costs of producing your product or service, which vary according to the number of units you sell

The costs of running the business, regardless of how much you sell

The investment costs of long-term tangible and intangible assets spread out over their useful life

The famous "Bottom Line"

	Sales	3,500
→	Costs of Goods Sold	-600
	= GROSS PROFIT	2,900
→	Operating Expenses	-6,200
	= CASH OPERATING PROFIT	-3,300
→	Depreciation	-300
→	Amortisation	0
	= OPERATING PROFIT	-3,600
	Interest	0
	= PRE-TAX PROFIT	-3,600
	Tax	0
→	= NET PROFIT	-3,600

← Total sales revenue from all products and services

← The profit you make from selling, excluding the cost of running the company

← The profit you make from your operations, before accounting for non-cash expenses

← The profit you make from your operations, before accounting for financial considerations such as interest and tax

← Only the interest payable on loans, not the repayment amount is relevant to the Profit and Loss Statement

← The tax you must pay on any profit you make