

Benefits of Benchmarking

Financial benchmarking measures the quality of an organization's processes, products, programs, and strategies and compares them with a standard measure or similar measurements of peer groups. The objective of benchmarking is to determine what and where improvements can be made to improve performance.

What Benchmarks to Use

These are a few of the key benchmarks that should be analyzed together to provide a quick and high-level review of a company's health.

- **Net Profit Margin**
 - *Net Profit Before Taxes Divided By Sales*. This metric is the most important as it measures profitability.
- **Liquidity Ratios**
 - **Current Ratio** *Total Current Assets Divided By Total Current Liabilities*. This metric shows the company's general liquidity, but it has some limitations. By including inventory in the calculation, it may provide a distorted understanding of the company's very short-term cash flow.
 - **Quick Ratio** *(Cash + Accounts Receivable) Divided By Total Current Liabilities*. This metric may not be perfect for gauging liquidity, but it is a useful and popular comparison to pair with the current ratio.
- **Turnover Ratios**
 - **AR Days** *(Accounts Receivable Divided by Sales) Multiplied By 365*. This metrics roughly measures the number of days a company takes to turn accounts receivable into cash. Lower numbers are desirable since it is better to have cash in the bank than extra receivable accounts on the books.
 - **AP Days** *(Accounts Payable Divided By Cost of Goods Sold) Multiplied By 365*. This metric indicates the number of days a company takes to pay its vendors. Higher numbers are better because it means the company is able to hold on to cash longer.
 - **Inventory Days** *(Inventory Divided By Cost Of Goods) Multiplied By 365*. This metric measures the number of days it takes to sell inventory and is specific to industry. For example, a winery will have longer inventory days than an egg distributor. Generally lower numbers are better.

These are common benchmarks used in financial analysis and can be used in combination with additional industry specific key performance indicators (KPIs). The work doesn't end once the benchmarks are completed. Use these metrics to determine where the company is excelling and potential problem areas. Use benchmarks as an opportunity to improve the company's overall performance.

SVA can assist you with benchmarking your company against your peers and industry standards.

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