

KPIs: What they are and why they're important

Stay on top of your business's long-term performance by monitoring key metrics...



Your quick guide on why KPIs matter to your business

We are happy to see you here digging into another educational resource developed to offer valuable tips on the importance of KPIs (key performance indicators).

While every business is a little different and will monitor their own unique set of indicators, it's important to understand the vital role these metrics play. Regular analysis of certain indicators (e.g., net profit and customer conversion costs) help business owners identify potential issues early on and make improvements to better ensure long-term financial success and sustainability.

We are here to help. So, if you have questions or would like to consult with a member of our team, please reach out to our firm today.



What are KPIs?

Key performance indicators (KPIs) refer to a set of quantifiable measures used to gauge a business's long-term performance (versus a set of targets or objectives).

KPIs specifically help determine strategic, financial and operational achievements within a company. KPIs can also be used to compare a company's performance to other businesses within the same market space.

What is the purpose of KPIs?

KPIs provide clarity on whether your business is on the right track for success. Are you profitable? What is the lifetime value of your average client? What is your churn rate year-over-year? And, if you are not successful in a given area, what can you do to improve performance?

The type of business and/or industry you are in will dictate which KPIs are most important to monitor and measure. For example, a software company looking to grow faster than its competitors may consider year-over-year revenue growth as its main performance indicator. A retail chain might place more value on same-store sales as the main metric to gauge growth.

Ultimately, the aim of any KPI is to bring about improvement and identify areas where KPI goals are not being met.

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The value of KPIs...

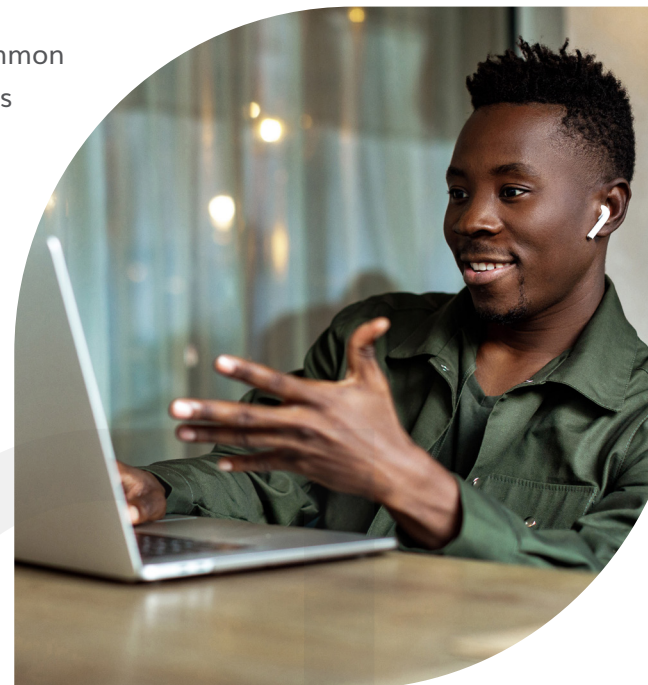
While we've narrowed the following list down to four key value propositions of KPIs, there are many more reasons why measuring certain metrics are important to your business. The following points are intended to serve as a starting point on your road to KPI higher education.

Monitoring your business's financial health

KPIs serve as a scorecard of sorts on the health of your business. The metrics you choose help track specific "vital signs" over time and ensure you are always working to meet set financial goals. Selecting the right KPIs is critical in order to measure the areas of your company you want to move forward and then put the needed resources behind to make that happen.

Depending on the business type and industries served, your metrics will be unique to your company. To effectively measure financial health, many business owners use the following common KPIs to guide them:

- **Net profit:** This involves tracking your net profit year over year. Of course, your goal should be to increase profits each year. Net profit is calculated as follows: Revenue - Expenses.
- **Net profit margin:** Net profit margin measures the profitability of your business and is also an indicator of how well revenue is being used. It's a measure of how much profit your business makes from the revenue it earns. The formula to calculate net profit margin is: $\text{Net Profit} / \text{Revenue}$.
- **Cash flow:** A healthy cash flow ensures that a business can pay common expenses such as salaries, utilities and taxes while also having funds to put toward growth and business expansion. Tracking this KPI allows you to better plan for large expenditures, keep spending in check, and offer lenders a clear picture of the business's financial health should you need to apply for a loan.
- **Customer lifetime value:** This KPI answers the question of how much a customer is worth. It's an important metric to monitor because it helps guide you on properly allocating funds to areas like sales and marketing.
- **Conversion rate:** This metric measures the number of prospects who actually convert to customers. There are many ways to measure conversion rate, depending on your business model. Reach out to our firm if you have questions on how to calculate this KPI.



Measuring progress over time

KPIs, if tracked consistently, are the best way to measure business progress over the long term. Companies can track everything from revenue, gross margin and employee turnover to customer churn, client conversion rate and more. Whatever the metrics you choose to monitor, the key is to measure progress toward meeting your set goals.

The fact is that you can't know where you want to go with your business if you don't know where you are currently. Key performance indicators help you understand your current state of business in order to set reasonable goals and objectives moving forward.

Solving problems and identifying opportunities

The right mix of KPIs in your dashboard provides you with current and accurate data at your fingertips. Having this information readily available enables you to proactively identify issues (and then solve them early) as well as identify new opportunities.

In relation to potential issues, for example, if you track cash flow and notice it's down by 20 percent in one month, you can adjust your sales and marketing efforts to accelerate inflow of cash in the coming months. Actions taken might include increasing the number of outbound calls, attending more selling/networking events or enhancing your client communications. Catching an issue early enables you to pivot quickly and solve what could be a bigger issue down the road.

KPIs are also a good way to identify new opportunities. For example, if you detect that customers often buy certain products in pairs, this could be an opportunity to bundle products and accelerate sales of multiple items at once.

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Analyzing patterns over time

If you measure the same KPIs month to month, you will begin to detect patterns in your data. There are countless ways these patterns can help you increase business success. For example, analyzing the data regularly may allow you to predict your slowest sales periods and periods of increased product demand.

So, if the data indicates that January and February mark a common slump in sales, you can adjust operations as needed. This might include increasing digital paid advertising during these months or running sales promotions. It might also include reducing staff during this time to decrease overhead in the short term.

On the positive side, you might identify periods where sales on specific products increase significantly. You could determine this is due to such events as college students returning to school or the launch of tourist season. This allows you to better predict demand on those products and ensure that you have plenty in stock during peak sales periods.

Final thoughts...

KPIs are not a new concept. The value of measuring business metrics is an age-old tactic that supports progressive improvement of operations and overall business success.

Using KPIs to measure certain aspects of your company offers immense value in terms of providing data insights and the ability to predict trends and circumvent possible issues. If you've yet to use KPIs to help advance your business, start today and start with the tips in this eBook.

Have questions about the value of KPIs for your business?

Contact us today! Simply click the **GET IN TOUCH** button on our website and complete the brief form. Remember, we are here to help!

