Financial performance measures

These five common financial performance measures or indicators are useful for co-operatives to be able to assess performance at different stages of co-operative's development.

Financial performance measures

Financial Indicator	Description
Return on capital employed %	Used to demonstrate the value that an organisation gets from the net assets held
Net profit % of member funds	A measure of the profitability of the organisation
Gearing %	A ratio that compares owner's equity or capital to borrowed funds. Gearing is a measure of financial leverage demonstrating the degree to which an organisation's activities are funded by owner's funds versus creditor's funds.
Net profit distribution to members %	The amount of profit shared by the organisation amongst its members.
Return on work done %	Used when there is little capital but there are employees and/or volunteers whose effort is notionally measured at a wage rate

Return on capital employed.

The return on capital employed, measures the value obtained from assets that the co-operative has. If the co-operative has very few assets, particularly during the start-up phase then making this calculation will be only useful as a point from which to show growth.

This measure is calculated by dividing net profit, that is gross income less costs and expenses, by net assets, that is gross assets less liabilities.

A co-operative with a net profit of $3,000 and net assets of $40,000 will have a return on capital of 7.5%, which demonstrates that the organisation is making a good return on the assets that it is using.

A start-up may have a loss in the first year and may have little in the way of net assets, as much of the cash has been paid out for product or expenses.

If there is a loss of $2,000 and net assets of $10,000, the return on capital employed is -20%. This will appear as a very poor financial performance measure, however, it is still worth recording to show progress.

It may take a couple of years for the co-operative to achieve a good return on capital.

Net profit as a percentage of members' funds

This is a useful measure for the start-up phase. It is a measure of the return on the amount that a member invests in share capital. This measure will only have significance for co-operatives with a share capital.

It is calculated by dividing **net profit** by **member funds**.

It shows the return on the amount a member invests in share capital. This is not a measure or indicator of dividends for members.
During the start-up phase, members will be comfortable to see profits reinvested to ensure that operational systems are established and bedded down to support growth. The measure tells the board and members how hard their investment is working.

Gearing ratio

The gearing ratio or debt to equity ratio is used to demonstrate the degree to which the activities are funded by members or creditors.

It is calculated by **total debt** divided by **members' share capital**. This measure will not have meaning for co-operatives without share capital and those that do not have any debt. A high gearing ratio will indicate that the co-operative is less reliant on member capital and this may impact on the co-operative's autonomy. Whilst creditors do not have any voting power in a co-operative, a high level of debt will influence the direction of the co-operative and impact on its ability to adequately serve members' interests.

Net profit distribution to members

Members that company shareholders do. Certainly, during start-up, it is unlikely that any corporation will be in a position to deliver dividends on shares.
Co-operatives, being designed to deliver products and services to members, will strive to deliver value very quickly. For example, a co-operative formed by small businesses seeking to access cheaper goods and services will be able to show the delivery of value to their members very quickly. Under this financial performance measure distributions of rebates or discounts based on transactions with members are included in the calculation of net profit distributions.

The **net profit distribution to members** may still not be a good financial performance measure in the early stages of a co-operative's establishment, but it can provide a strong indicator of member value and demonstrates how well the organisation is meeting members' financial expectations.

It is calculated by dividing the **payout to members** in the year by the **total of member funds**, this gives you a percentage of the return against the members' investment in the co-operative's share capital.

As the co-operative grows and develops its volume of transactions with members, this measure will show the benefit of member share capital staying and growing within the co-op. It will become a key indicator to retain members and attract new members.

Return on work done

This financial performance measure is the one that probably makes most sense to small start-ups where boards have to work hard to get the business up and running!

The **return on work done** measures the value achieved by all those long hours of work by directors, members and staff.

Often a start-up will have little capital and will rely on a mixture of paid and unpaid hours provided by members. It is useful to record these volunteer hours by using a notional wage for these hours to get a total cost of work done.

Having a cost of total work done will also be useful when deciding if some or all the volunteer hours can be replaced by paid hours.

By giving this time a value, it is possible to calculate **a return on work done** by dividing net profit by the cost of work done.

This is a useful measure at start-up because a lot of the work done in the first year is about setting up the organisation to succeed;

- finding customers and suppliers and developing good relationships with them,

- working out which of the co-op's production and delivery systems work well and which don't.

This work will add excellent value, but not necessarily dollars, to the co-operative enterprise.
This is value that is not counted as an asset, and is frequently only seen as cost, but it is value of which that the co-op's members should be aware. It can contribute to retaining loyalty where members see how their co-operative is committed to working to deliver member value.