

What is the Cashflow Quadrant?

The Cashflow Quadrant is the title of a Book by Robert Kiyosaki of “Rich Dad, Poor Dad” fame. Now to be perfectly honest, I found the book a bit hard going. I had previously read “Rich Dad, Poor Dad” and I think that I was simply over Robert’s writing style. This being said, I did find the concept incredibly powerful. It is a concept that I have used endlessly as a Business Advisor with my clients and prospects, to help them understand the importance of growing and structuring your business so that it runs without you.

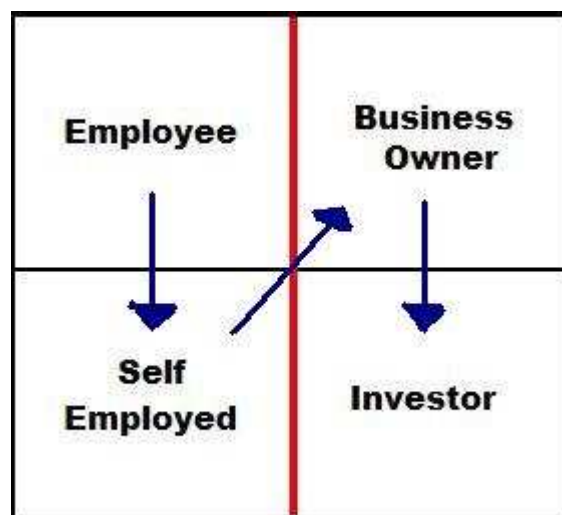
Are you are Business Owner?

A common Business Coach/Advisor line is to ask a prospect if they are a true Business Owner. The definition we give them to gauge this against is: “Can you go away on a holiday (or get hit by a bus if you really want to create drama) for 3 months and when you get back, your business has not only survived, but prospered? The answer to this is almost always “No”. This then leads us to explaining to them about how we can help them become a true Business Owner.

Now this is a great way to get people thinking about whether their business provides security. But it doesn’t really explain the real impact on your overall wealth. This is where the Cashflow Quadrant comes in.

So enough dribble, “what exactly is the Cashflow Quadrant”?

The Cashflow Quadrant is:



This essentially shows you the normal flow of someone starting out and building their own business. It is broken into 4 quadrants as well as 2 halves, with each area having its own unique characteristics. So let’s start with the quadrants and move onto the halves.



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Employee

An employee is where most of us start out. It is where we work for someone else and get paid for our efforts. If we put in the effort, we are rewarded by our employer with a wage. If we don't put in the effort, then we face the prospect of losing our job (i.e. not get paid). It is usually low stress, as short of losing our job, we are pretty secure and get paid every week regardless of what's happening.

Self Employed

This is where we usually go to when we decide that we want to work for ourselves. It is very similar to being employed, except that we are also responsible for paying our wage. The main reason it is similar, is that we are rewarded for our efforts. That is, if we go out and get ourselves a new client/customer, then we will get paid that week. If we don't, we won't. So we are essentially getting paid for the work that we put in. If we don't put in the effort, then we don't get paid. The main difference is the stress levels. Unlike the Employee, we are 100% responsible for our success. When times are tough, this can be very stressful. This unfortunately, is where most people running their own business stay.

Please note: The number of employees you may have has no bearing on whether you are classified as self employed. If you are still required to work in your business everyday to ensure that the money keeps coming in, then you are Self Employed.

Business Owner

Now we're getting into the good stuff. A Business Owner is where you get rewarded for other peoples' effort. That is, you surround yourself with a team of people, who look after all the day to day activities in your business. This not only includes providing the Goods & Services, but generating the sales and growing the business. Your role is simply to provide strategic direction and decide where the profits should be spent. Now the stress levels could be high, but generally they are lower than being self employed as the success of your business is not 100% on your shoulders (as long as you surround yourself with the right people).

Investor

Unlike a Business Owner, an Investor has no real input into the running of the Business they invest in. They are purely an Investor and the only decisions they make are which businesses they should invest their money in and when to pull it back out again. The best example is someone who invests in the Share market. The stress levels here are non-existent, providing you've invested in the right businesses and the money will just come in.

Now to the real power of the Cashflow Quadrant – Leverage!

What is Leveraging?

The 2 halves of the Cashflow Quadrant are defined by the level of Leverage. As an Employee or Self Employed, you have very little leverage. This simply means that any financial rewards you receive are directly proportional to how much effort you put in. In other words, your earning capacity is capped by the number of hours you can put in. If you can't work anymore hours, then sooner or later your income will stall. To prove this point, as well as that the number of employees has no bearing on whether you are self employed or a business owner, I will give an example.

As a Business Advisor, I worked with a client who had built up their business from scratch to a turnover of

\$6 million dollars and employing 15 staff. Unfortunately, after many years of great growth, the Business Owner (or so he thought he was), had stagnated at that level for several years. The reason was that they were working 70-80 hours a week and couldn't physically put in any more hours. They couldn't employ anyone else to help, as they were too busy managing the staff they had. They physically didn't have the time to employ, train and manage additional staff members. As it was, they were losing control, which meant that some jobs were being finished over time and over budget. Now it doesn't take Einstein to work out that this could only lead to problems down the track. What he needed to do was start replacing himself in the Business, so that he could become a true Business Owner. The business then wouldn't rely solely on his input and could then continue growing.

This brings us the other half of the table. The Business Owners and Investors half is highly leveraged. This means that your earning capacity is uncapped. As the Businesses you're associated with continue to grow, so will your income. In other words, your income is a result of other people's effort. The more people working, the more money you will make. Some of this you will have direct input into and some you won't.

So where do you want to be?

I would hope that like me, you realise that the right half is where we should be. After all, why go through the pain of starting your business if you are not going to be rewarded nicely for it. But to get to the right side, you must first work out exactly where you are now – and be honest (you are only lying to yourself). Then work out what actions you need to take to get over there.

One final note!

The reason there is a big red line between the 2 halves, is to signify difficulty. It is reasonably easy to move between Employee and Self Employed or Business Owner and Investor, but difficult to move between Self Employed and Business Owner. That's why there are far more small businesses owners that are Self Employed rather than Business Owners. There can be a lot of pain getting over the red line. I'm sure you've heard a small business owner say that "we used to have more staff, but it was too hard and we were making less money than we used to, so we went back to just me and ? other staff". Basically, they got on top of the wall and gave up, falling back to where they started.

So work out where you are at, where you want to go and start taking action to get there. Be prepared for pain along the way, but know that it will be worth it when you get there.