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Thriving in Volatile Times

Get and keep your business on track

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would benefit from reading it.**

Thank you.

We seem to be in the midst of an economic “perfect storm.” Escalating oil prices add to costs across the board. The global nature of our supply chain means issues on the other side of the world impact costs close to home. A weak dollar increases the cost of imports and lowers the price of American goods abroad. Home values are dropping, further eroding confidence and curtailing consumer spending. Many companies are seeing flat or declining revenues coupled with increasing costs.



Stop doing more of what isn't working or taking a “shotgun” approach.

Case Study: Simply Candles

Renee Coty, the owner of an established retail company, recently sought help after two years of declining revenues. Despite significant growth in Web sales, the bottom line was slowly eroding.

She had reacted to waning profits by working longer hours to reduce staffing costs and was considering adding new products, hoping for a moneymaker.

She was doing what she had always done but expecting a different outcome.

Doing more of what isn't working or striking out in many possible directions at once - hoping that something will click - is unlikely to help. Success, especially in volatile times, requires focus, discipline and commitment.

Next learn how to improve your company's bottom line.

**Businesses are more profitable when their owners
regularly ask and systematically answer two questions:**

What's making money?

What's dragging down the bottom line?

When times are good, you may tend to be swayed by the timeless advice of "if it isn't broken, don't fix it." If business is slow or profits are declining, you may hesitate to stop *any* revenue-generating activities, including those with little or no profitability.

Following these natural tendencies might cause you to miss important insights into how to make your business stronger.

**Revenues from profitable activities can mask
the drain of unprofitable ones.**

Resources used to pursue unprofitable or marginally profitable activities could generate better returns or set up the company to prosper when times improve.

Figuring out which activities are profitable can be relatively simple. Most companies have the necessary data but haven't organized it in a way that provides useful guidance.

See how to uncover the profitable and unprofitable parts of your business.

Try this four step process.

1. **Assess the relative profitability of each aspect of your business.** Systematically answer these questions: What's making money? What's dragging down the bottom line?
2. **Evaluate your company's strengths and weaknesses** and how it compares to the competition on products, service, price, and other factors that determine whether the customer buys from you or someone else.
3. **Consider environmental threats and opportunities.** How might demographic trends impact your business?
4. **Create a detailed, measurable plan to guide your company.** Involve the right people. Measure your progress and make appropriate mid-course corrections.



Caution: What you don't know can hurt you.

Step One: Assess Relative Profitability

Create a structure for your assessment

One essential tool for monitoring profitability is an income statement, commonly called a P&L (profit and loss), which lists all income and expenses for a period of time. This report shows how a business is performing overall; but, is that the whole story?

Are all aspects of your business equally profitable? Dig deeper to gauge the financial health of the separate parts of your business. Consider lines of business, products and services, target markets and distribution channels.

Create a structure for your assessment. For example, if you wonder whether a particular market segment is profitable, separate income and expense by market. Or, if you question the viability of certain products or services, group accordingly.

Simply Candles Background



Simply Candles, owned by Renee Coty, is a small retail sales firm that sells decorative candles and accessories through three channels: a small storefront, by telephone and via the Web. Repeat sales account for 60% of volume. Recently, despite significant increases in Web sales, net income is declining.

Simply Candles sells a wide range of candles from high-end to value-priced, commodity candles. They are the sole importer of a unique line of candles and matching accessories. Pricing is cost plus and the same percentage is used across the board.

Two part-time sales reps staff the phones and store, earning 30% commission on those sales. Another part timer picks, packs and ships telephone and Web orders five afternoons a week; accounting, HR, and marketing duties are outsourced. Renee, the owner, oversees the operation.

Renee's compensation (\$45K owner's draw and benefits) pays her bills, but she's concerned that despite top line growth, her company's bottom line is shrinking.

Analyze income and expenses based on the structure

Using your company P&L, separate income and expenses based on the structure and the period of time you chose.

Include both fixed and variable costs. For example, retailers' variable costs generally include purchased goods, inventory carrying, staff compensation, card processing fees, packaging, and shipping. Fixed costs include storefront, (whether real or virtual), utilities, and communication equipment.

Don't overlook what's spent on marketing, accounting, HR, management, investment in property, plant and equipment and a reasonable cost for owner's uncompensated activities.

Where costs support sales of multiple offerings or products and services in more than one category, apportion them

using some reasonable estimate of their impact on your overall business, for example, as a percentage of sales.

Don't let the pursuit of precision derail or delay your effort; an estimate is sufficient.

Write down your assumptions and review them when you repeat this exercise; with practice, your estimates will become more accurate.

Remember, tallied costs for all products and services or categories for a given period should match the income and expenses shown for that period on your overall P&L plus whatever uncompensated owner's time was contributed. Use this method to create a "mini-P&L" for each product and service or other category.

Sound complicated? It really isn't. Find out how Renee got started.

Simply Candles' Mini-P&L

Review of last year's results informs Renee that the first question to answer is how profitability differs across sales channels.



Renee adds three additional columns and allocates all of her costs across the three different channels, noting her assumptions.

Clearly, Web sales carried the rest of the business in 2007. But would overall profitability be improved by eliminating the store and/or telephone sales channels?

		Total	Store	Web	Telephone	Assumptions
Gross Sales		\$275,000	\$50,000	\$125,000	\$100,000	
% Gross Sales		100%	18%	45%	36%	
Cost of Goods	% GS					
Purchased goods	35%	\$96,250	\$17,500	\$43,750	\$35,000	Mark-up is same for all
Card processing	2%	\$5,500	\$1,000	\$2,500	\$2,000	
Packaging	1%	\$2,750	\$500	\$1,250	\$1,000	
Shipping	10%	\$22,500	\$0	\$12,500	\$10,000	
Commission	30%	\$45,000	\$15,000	\$0	\$30,000	No commission on Web sales
Total COGS	78%	\$172,000	\$34,000	\$60,000	\$78,000	
Gross Profit		\$103,000	\$16,000	\$65,000	\$22,000	
Indirect Cost						
Store rent		\$7,200	\$4,320	\$0	\$2,880	Retail 60% telephone 40%
Warehouse rent		\$4,800	\$873	\$2,182	\$1,745	% of sales
Utilities		\$2,400	\$436	\$1,091	\$873	% of sales
Telecomm		\$2,400	\$400	\$1,000	\$1,000	Store \$400; split remaining
Marketing		\$10,000	\$1,818	\$4,545	\$3,636	% of sales
Accounting		\$5,000	\$909	\$2,273	\$1,818	% of sales
HR		\$3,000	\$1,000	\$1,000	\$1,000	1/3 to each
Owner's Draw		\$45,000	\$15,000	\$15,000	\$15,000	1/3 to each
Insurance		13,800	450	450	450	1/3 to each
Other		\$8,000	\$2,667	\$2,667	\$2,667	1/3 to each
Total Indirect Cost		\$73,800	\$9,756	\$31,591	\$32,453	
Net Income		\$9,700	-\$13,256	\$33,409	-\$10,453	

Ready to start your analysis? Here are some questions to get you going.

Use the mini-P&Ls to reveal the current relative profitability of your offerings, reconsidering the 4 Ps of marketing – product, price, promotion and place. Start your analysis with these questions:

- *Can anything be done to reduce expenses, e.g., better inventory management, different hours of operation, more efficient manufacturing practices, improved supplier contracts or streamlined workflow?*
- *Are your prices aligned with customers' perceived value of your products and services? Can you raise prices on offerings unique to your company? What is the competition doing? Are you selling in the best possible market?*
- *How will paring back offerings impact those remaining? Could this disrupt the pipeline of customers? Or allow investment in sales with better margins or potential?*
- *How will changing the product/service mix impact cash flow? Do you need to transition to different offerings or markets and/or scale back your operation?*

Find out next what Renee concluded from her analysis.



Renee's Analysis of Sales Channels

It's clear to Renee that store and telephone sales are not currently profitable; but, this isn't the whole picture. Many of her customers have said that they prefer to call rather than order over the Web; eliminating telephone sales is not an option. However, she is seriously considering closing the store.

Renee will analyze telephone and Web sales to see if they were largely re-orders of products first purchased in the store. She wonders if making the first sale depends on the customers seeing and handling product. If so, she'll consider more cost-effective ways to get her products in the hands of customers, such as sampling or co-marketing, placing her candles at retail outlets (e.g., high-end spas, hair and nail salons) where her target customers regularly shop.

Sales staff are paid commission only. Will increased telephone sales make up for the loss of \$15K in store-based commissions? Renee wants to keep two part timers as they cover each other's time off, know the product line and are valued employees. Both are happy with their hours and pay.

To keep current staff, her model will need to generate the full \$45K for sales staff compensation.

Renee uses the same mark-up on all the products she carries. Repeat sales of the high-quality line she alone imports are growing while sales of low-end goods are slipping. Her competition is deeply discounting to boost flagging sales. Renee plans to raise prices on her high-end goods and consider cutting back or even discontinuing sales of low-end candles.

The store and warehouse are located downtown on a busy street with relatively high rent. Pick-up and delivery vehicles are hampered by traffic. There's no loading dock, so goods shipped to her site cannot be delivered on pallets. If the store closed, the company could move to less expensive quarters optimizing their location for ease of shipping and receiving.

Before taking action, Renee will develop expense and revenue projections to assess the impact of any changes.

Step Two: Evaluate your company's strengths and weaknesses

Consider your company's strengths and weaknesses *in context* - most broadly, in relation to your ability to fulfill your mission and achieve your vision or, more narrowly, how well positioned your company is to meet your current business objectives. Be systematic and conduct your review in light of environmental opportunities and threats.



Gain multiple view points by involving others.

- How do you as an owner see your company?
- Is that different from your customers' view?
- How about from the standpoint of an employee, supplier or vendor?

How does your company stack up?

- *Track record:* Delivery on warrantee, timeliness, alignment with stated values, community perception
- *People:* Employees at all levels, length of service and expertise of current staff and the pipeline of future workers
- *Physical location:* Facilities, operating hours, accessibility, convenience, work flow, flexibility to re-size (up or down)
- *Products and Services:* Quality, relevance to customers, range of offerings, price/value, adaptability to different markets



- *Customer base:* Loyalty, growing/shrinking, level of integration with your company
- *Suppliers:* Reliability, financial viability, integration to your supply chain, distance from your operation
- *Capitalization:* Debt position, cash flow, credit worthiness, line of credit
- *Board of directors/advisors:* Expertise, ability to make connections, commitment to your success

Step Three: Consider environmental threats and opportunities

For your company, in light of your plans and your geographic reach, do these present opportunities or threats?

- *Demographic trends:* Think about your target market and how changing demographics might impact your company, considering age, gender, education, family status, income, population increase/decrease, mobility, and needs.
- *Psychographic trends:* What are your customers' likes, dislikes, and values? Do they have access to and use the Internet?
- *Economy:* Is the economy in your area growing, shrinking, or flat? Does the value of the dollar or other currency impact your company? How about the current credit market?
- *Competition:* Is your competition growing, shrinking, or stable? Typically, what is their value proposition? How easy is it for a company to enter your market?

Assessing strength, weaknesses, opportunities and threats (commonly called a SWOT analysis) is an iterative process done within a context. Document your assumptions. Review it regularly.

See how Renee did her SWOT analysis



Simply Candles' SWOT Analysis

Strengths

Weaknesses

Internal

- Relationships with suppliers; some exclusive
- Efficient, low staffing costs
- Loyal customer base; high % repeat orders
- Complete line of candles and accessories – one-stop candle shopping
- Name recognition
- Sales channels (Web and telephone are complementary and drive traffic to each other)
- Capitalization (e.g., no debt)

- Relatively high overhead (store)
- Cost plus pricing structure (all mark-ups the same) doesn't reflect market value
- If store is closed, need way to introduce high-end products
- Little bench strength; loss of any employee harmful
- No back up for owner/manager
- Little available revenue to invest in growth

Threats

Opportunities

External

- Competition pricing "commodity" candles lower; can/will steal market share
- Competition could duplicate "exclusive" products from less costly supplier
- Barriers to entry of competition relatively low
- Suppliers could become competitors (e.g., sell retail)
- Increase in shipping expenses will increase cost basis
- Weak dollar will increase cost of imports (in dollars)

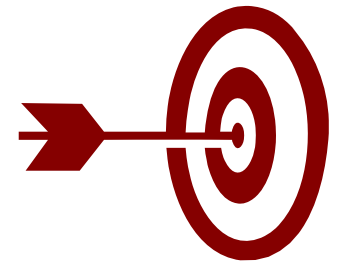
- Create custom candles for businesses to give as client gifts; could easily imprint client logo on packaging
- Co-market with overseas candle company to help raise awareness of their brand and Simply Candles as an exclusive outlet
- Place candles at spas, hair and nail salons for display/sales to replace retail store
- Sell candles & accessories at home shows and other outlets
- Position candles as inexpensive "luxury" in poor economy
- Suggest candles be replaced 4 X year (consumable, seasonal, color and scent fade in time)

Step Four: Take action and monitor your progress

Share the results of your analysis; work with all affected employees to determine feasible plans. Seek input from customers and suppliers. Consider involving your banker and professional advisors. You may learn additional factors that should be considered. Create a plan with clear goals, measurable milestones and defined roles and responsibilities to guide the transition. Be sure to identify an individual to manage the plan and report progress.

Is your business present where your target customers shop?

Know your target customers and market(s).
Create plans with the customers' perspective in mind.



Do your marketing materials communicate well with them?

Plan promotions that catch the attention of your target customers. Don't restrict yourself to traditional advertising; consider co-marketing, sampling, and event sponsorship. Evaluate whether a Web presence or improvements to your existing Web site could make a significant difference.

Assess your pricing practices

Price your product above the fully allocated cost of goods sold, plus a reasonable profit, but remember: the price ceiling is market value. Are any of your products and services unique?

Don't let a formulaic cost-plus approach blind you to profit potential.

Pricing is a balancing act. Pay close attention to both financial and market trends. Review your prices often to maintain your profitability.



Do your products and services meet – *or better yet* – exceed your customer's needs?

How can you learn this? Ask.

Talk to your front line sales, technical support and customer service staff. They interact with your customers daily and have first hand, up-to-the-minute information.

Analyze returns and warranty claims. Look for trends. Are there product quality issues? Do customers have needed information and an easy-to-use process to select the correct product – size, features, and capabilities? Do customers know how to properly use your products?

Create feedback mechanisms and listen to your customers. Do you ask each new customer how s/he learned about your company? Do you ask returning customers what they like most about your goods? Have

you asked whether your customers would refer your company to others?

Monitor customer retention; if you're losing customers to the competition, ask why.

Do you have an "ideal" customer relationship (e.g., long lead time on orders, use your full range of services, follow a certain order process) and actively use advantageous pricing, improved turnaround, and clear communication to encourage that interaction?

Size your company to operate efficiently.



Stop activities that don't support your plan.

A line of business that generates great cash flow but poor or no margins is hard to abandon. However, unless you can significantly lower cost and/or increase price, you may not have a choice. How much time and energy is spent performing unprofitable work? How much money is tied up in inventory, parts and equipment? Make a plan to transition to more productive activities.

Actively seek ways to operate more effectively.

Common sense tells us that the person doing a job is a great resource to identify what might be improved. Many companies have developed formal employee suggestion programs to take advantage of this idea. [Read more.](#)

Periodically review your processes and work flow. Ask why each step is performed. "Because we've always done it" is not a good reason. Eliminate non-productive steps.

Assess whether your systems support your ideal work flow and processes.

Monitor your results.

Pick measures that are easily understood and represent actual progress.

Determine how to track the impact of planned changes. Measure at intervals that allow enough time to see differences yet avoid drift. Commit to sharing results (good or bad) with employees.

Based on results, make needed mid-course adjustments.

If your plan calls for sales of \$50,000 a quarter and you're at \$5,000 after a month, decide whether to stay the course, increase efforts, change the plan or lower expectations.

Use your plan to guide and measure your progress.

Measure the impact of your actions at reasonable intervals by including mini-P&Ls as part of your regular reviews of operational and financial results. Ensure that your actions are having the desired effect and changes in one area are not causing problems in others.



Simply Candles...the rest of the story

After three months...

Renee decided to close the store and move five miles to a business park. The new site offered a loading dock, better Internet access, nearby interstate entrance and free parking.

Since telephone and Web sales were driven by reorders of store purchases, Renee and her employees brainstormed ways to allow customers to experience products after the store closed. They surveyed customers to learn which ideas would resonate. Many customers hesitated to buy expensive items sight unseen. However, a new sales policy – *Your money back for any reason!* - overcame objections. One regular store shopper made her own suggestion: open the warehouse for periodic weekend sales.

Renee raised prices on the high-end goods by 25%, letting her existing customers make one final purchase (before the move) at the old prices.

Over the years, the total number of products carried had grown along with inventory carrying costs. From her competitors' Web sites Renee learned they sold low-end goods at much lower prices. Her money back policy made competing on price unsustainable; she decided to stop selling low-end products. She ranked each of her remaining products by inventory turns and discontinued slow movers.

Renee hoped to finance her move with proceeds of the store sale by deeply discounting discontinued items.

Cost and revenue projections for planned changes showed commissions would drop for a time because of the move, price increases and discontinued products. Renee offered sales staff wages equal to their average weekly commission until sales rebounded.

One year later...

Simply Candles gets more favorable pricing by buying full pallet loads of goods. Inventory turnover is improved. By reducing and eliminating many costs, gross margins are up to 35%. Total sales have rebounded and are growing.

Employees love the new location; commutes are easier and parking is free. Telephone sales in dollars are up because of pricing changes and volume grows as a result of reduced wait time (no store customers). Sales staffers are back on commission and delighted with their extra income. Renee plans to add another part-time shipping clerk to handle the extra volume and offer performance bonuses for exceeding volume goals and meeting turnaround times.

Customers remain loyal; repeat orders are steady at 60%. Results of the first warehouse sale were encouraging; Renee plans to hold them quarterly.

Be patient and stay committed. It takes time to change a business.

Take heart from positive changes, even if they're small. Each step helps build positive momentum. Be the champion of change; keep your employees and yourself focused.



Volatile times can offer opportunities. Smaller, focused businesses can often take market share from large, complacent competitors. Well-run, established businesses can benefit when unfocused competitors go under, thinning the competitive landscape. Make a commitment that your company will be among those that prosper.

Laurie Breitner has 31 years' experience assisting organizations with strategic planning, change management, organizational development and operational improvement. She has worked in corporate management, consulting and education since 1977 in a wide range of settings and helped clients in insurance, financial services, pharmaceuticals, shipping, manufacturing, retail, education, the arts, community service and advocacy.

Laurie founded Breitner & Associates to help organizations work more effectively and successfully. Since 1991, clients have benefited from her unique ability to provide long-term perspective and planning as well as implement tactical solutions to complex business problems.

In 1985, Laurie earned an MBA with honors from the University of Massachusetts, where in 1973 she received a BA in Psychology cum laude and in 1977 was awarded an M.Ed. This distinctive educational background coupled with her broad-based business experience enables Laurie to provide clients with a multi-discipline perspective to problem solving.

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