HOW DO WE MAKE MORE PROFIT?

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Profit is an outcome. It's the end result of the actions and inactions in your business. If you want to increase your profit, then you need to do things better than you have before. You need to be more effective and more efficient across all aspects of your business.

Easy.

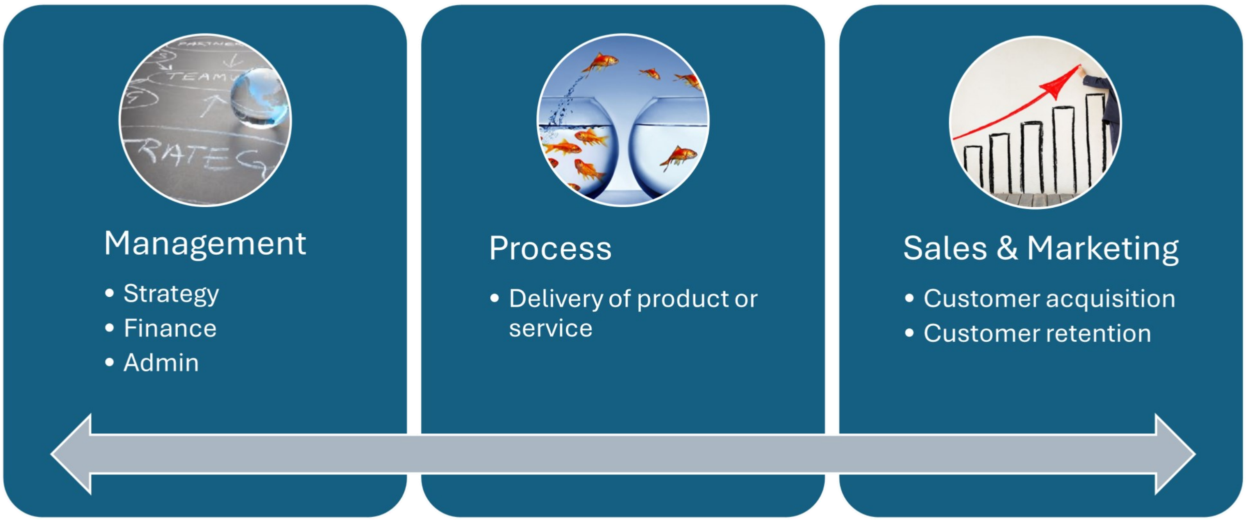
If only it was!

Let's look at the fundamentals of increasing profit.

The first thing to remember is that there is rarely a single, magic solution to dramatically increasing your profit. It can happen, but more often than not, increasing your profit is about doing many small things better than you have in the past.

Too often, businesses fail to maximise their profit because they ignore the small changes in their hunt for the one that makes a big impact. Those small changes, all added together and having an increasing impact as time goes by, quite often are the big impact.

Let's look at the three core components of any business



Management is how well and effectively you run your business. Process is what you actually do, your products or services. Sales and marketing is who you sell it to, in what quantities and at what price. We can look at profit through these three components.

Sales and marketing	=	Turnover
Process	=	Costs
Management	=	Best value

All 3 components need to be adequately addressed if any business is to grow successfully. Focusing primarily on process, as many businesses do, stifles growth because the lack of attention to the management and sales and marketing components adds barriers.

So it is with profit maximisation. Focusing in isolation on growing the top line, or on cutting costs, can bring short-term benefits but in the longer term can be counter-productive. Too many customers can increase non-recoverable costs such as overtime, returns, overstocking, etc. Cutting costs too far can restrict profit through lack of resources, poor-quality product, and so on.

Profit maximisation has to therefore be approached in the same strategic fashion as your business's growth plans. In getting more of the customers and sales, the emphasis has to be on getting the right sort of customers and the right sales in a cost-effective manner. Rather than looking at increasing your turnover, sales and marketing strategies should adopt a rounded approach, consistent with the management and cost strategies of the business:

Don't get any customer... get the right one at the right price and sell them the right things.

You see how this is a much more encompassing approach but also the most profitable. You are not wasting money on badly thought-out and poorly executed sales and marketing approaches that run the risk of bringing in non-profitable customers.

Anyone can pick up new business. Dramatically undercut all of your competitors, massively advertise the fact and you'll get loads of new customers... but will you make more profit?

Only if this is a carefully considered strategy and one that ties in with your management and process strategies. In other words, high volume and hugely efficient in everything you do. If that's not your business, then such a marketing approach would have a devastating impact on profit.

So, before you set about increasing your profit, you have to make sure that you fully understand all three components of your business strategy:

Process	What do we do best, what can we do and what shouldn't we do?
Sales and marketing	Who are our customers and what do they want?
Management	Who are we, what are we and where

Once you are confident in your ability to answer these questions, then, and only then, are you in a position to really set about increasing your profitability.

1. Increasing your profit from sales and marketing

You'll notice that we've deliberately not headed this as 'increasing your turnover'. It may be the answer but not necessarily so. Remember, sell the right things to the right people in the right quantities for your business.

Sales and marketing is the subject of many a book and too lengthy on area to cover here. However, look out for future e-books!

2. Increasing your profit by controlling your costs

Again, you'll notice we've not headed this as 'cutting your costs'. There may be times in any business when you just have to save the cash and cut your costs but that's a reaction, not a strategy. If it has to be done, then it has to be done, but it should never be anything more than a short-term survival measure.

In the same way that your sales and marketing is most profitable if it is planned and controlled in a manner that is right for your business as a whole, so your cost control will have the most beneficial impact on the profitability of your business if it is done on a more rounded basis and not just focused on cutting costs.

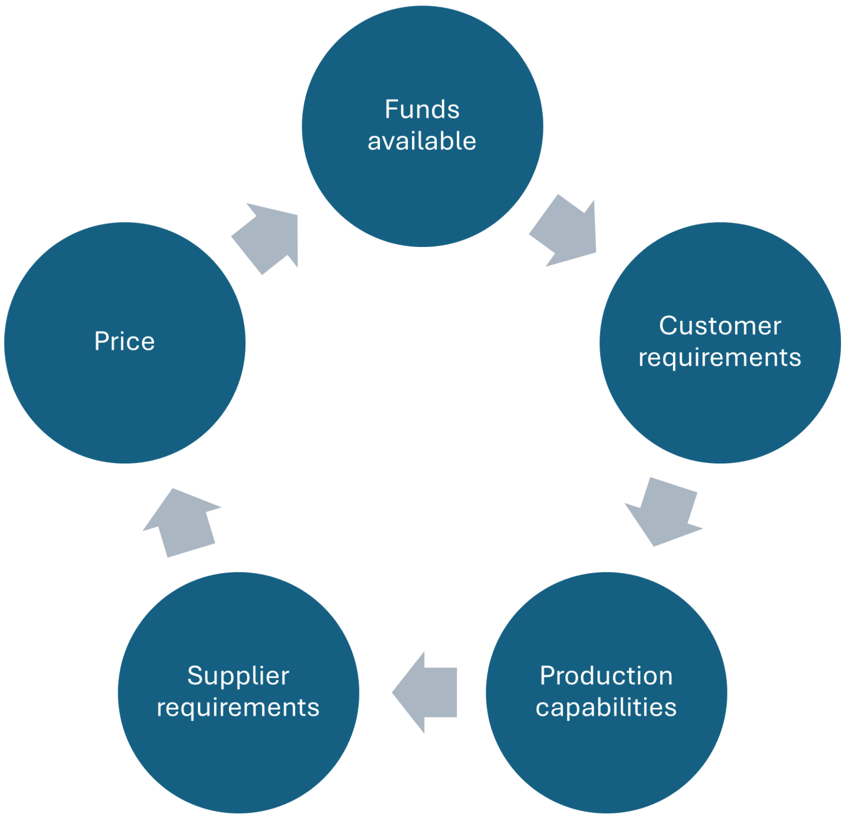
In essence, this means getting the most benefit per pound spent. It's better to spend £10 on something that will generate £20 of profit than it is to save £4 in the short term by spending £6 on something that generates only £8 in profit.

A 100% return on the more expensive unit compared to 33% on the cheaper version...providing, of course, that you don't just have £6 to spend in the first place.

This is where budgeting is so important. We covered this in our e-book "Why Do We Keep Running Out of Cash" and financial forecasts have to be the starting point for any cost control. You have to know what money you have to play with and how you intend to allocate it.

With your forecasts in place, look at the funds you've allocated to each specific cost and then set about achieving the best value that you can, i.e. the most benefit to your business, from those funds. Remember that you are looking at it in the round and not just with the tunnel vision of saving money.

The Hunt for Best Value



For each area of cost, you are looking not at what you could potentially save on price but what is available out there in the market place that will enable you to deliver what your customers want at the most effective price for your budget.

Go back to our example. If your budget allows you to spend £10 per unit and this delivers what your customers want for the most profit (£20), then this is the direction you clearly go.

However, if your budget doesn't allow you to spend £10, if it doesn't deliver what your customers want, if your people can't make it work or if it simply isn't available out there in the market place, then it's back to the drawing board.

Maybe the £6 product is now your answer, but again, only if it delivers what your customers want and there is nothing more effective out there in the market place.

It's a matter of

- Knowing your budget
- Understanding your customers' needs
- Understanding your own limitations and skills
- Knowing your supplier options

All of these are constantly moving pictures so cost control is not a once-a-year exercise and this is often where the avoidable costs start to creep in. Business managers will often source a supplier and then, providing the service remains reasonable, stay with them for many years without revisiting what is happening in either the supplier or customer market place.

Loyalty is a big thing. We look for it from our customers and our suppliers should be looking for the same. We're not advocating a constantly changing supplier list but it is important that your suppliers earn your loyalty by staying at the forefront of their market and continuing to supply you with the best possible deal out there.

It is fair and commercial for you to revisit your arrangements on a regular basis to ensure that you are still getting best value for your spend. Loyalty doesn't have to come at a price.

This brings another factor into play. Part of your equation is to ensure that you are sourcing supplies that help you deliver what your customer wants.

How does your supplier know what your customer wants?

How do you know if your supplier could help you better deliver what your customer wants?

The fact is, unless you help your supplier to understand the needs of your customer, then you run the risk of missing out on an opportunity to deliver better.

The price, quality, quantity and timing of delivery of your products and services to your customers are affected, directly and indirectly, by the price, quality, quantity and timing of delivery of your suppliers' products and services to you.

The better your suppliers understand your needs AND the needs of your customers, the more chance you have of the whole process being effective.

Of course, you have to be aware of any competitive elements and of any customer confidentiality needs, but it's worthwhile looking at your list of suppliers to see and judge who you can bring closer to your business and your customer's business for the benefit of you all.

Clearly, most businesses will have a wide range of suppliers:

- Small suppliers with a close relationship
- Suppliers with little relationship
- Large suppliers
- Regular suppliers
- Intermittent suppliers
- Key accounts
- 'Monopoly' suppliers

Cost control is not a 'one size fits all' approach. Determining the nature of the relationship, the degree of dependency and the suitability of resource is down to the skills and experience of the business manager and will influence just how much communication is possible and worthwhile.

We've not made reference yet to what, for many businesses, is their biggest cost... staff. Your work-force are suppliers like the rest of your purchase ledger, and in many respects, the same principles apply. Getting the best value from your team depends, in part at least, on similar factors:

- Understanding the requirements and skills of your staff
- Getting the most effective price level
- Understanding the recruitment market
- Ensuring staff understand your needs and those of your customers

This is a different slant on cost control, then. No longer are we looking at simply the cheapest option. Instead you run down your profit and loss account with a quite different checklist in place:

- Is this item of expenditure in line with budget?
- Is this line of expenditure necessary?
- Am I best meeting my customers' needs in this area?
- Have the terms and conditions of this supplier been reviewed recently?
- Is there scope for working more closely with this supplier?
- What else is out there?
- Can I simply cut the cost without affecting my customers?

We advocate a systemised process for everything. Cost control is no different.

You should establish a timetable for reviewing your costs in line with this checklist. How regularly and extensively will depend on the resources you have to hand.

If it's just you, then split your overheads into small groups and tackle a few every month. If you have some people available, then have either one person allocated to control the cost as a key function of their job or allocate the costs to different people according to their function.

However you do it, regular and systematic review within the framework of the checklist above will enable you to use cost control as a means of increasing customer service and raising profitability at the same time.

3. Increasing your profit by improving your management.

We've looked at the sales and cost factors of profit. In both cases, it's been a matter of looking at how those areas can be improved within the framework of the entire business and not just in isolation.

We've improved the profitability of our sales and marketing effectively by understanding our market place better.

We've improved the effectiveness of the pounds that we spend by taking what we know of our customers and looking at our supplies in that context.

So let's now look at the bit in between. Let's look at what happens when we better manage the processes that we control.

This may seem like a blindingly obvious statement but your business has more chance of being more profitable if you manage it more effectively.

For a blindingly obvious statement, this is probably the greatest failing in UK businesses today.

Ever heard the statement about "working on your business and not in it"? Of course you have. Do you follow it through?

The fact is that the vast majority of people managing small businesses in the UK today started that business NOT because they wanted to run a business but because they wanted to do what they do <u>their way.</u>

In other words, they were employed as an engineer but thought they knew a better way to be an engineer. They were employed as a designer but thought they knew a better way to be a designer. Sound familiar?

The driving force was to do a job a different way or to service customers a different way and the only way to do it was to set up on their own. Absolutely nothing wrong with this, we've pretty much all done it.

The problem is that we end up with really good engineers and really good designers trying to do a job they've not been trained for, which is to run a business.

We could write a book on this issue alone but let's look at it in the context of what we are talking about here. If you are going to make a profit, then you have to do what you do in the most efficient and effective manner. If you use other people, systems and processes to do what you do, then you have to ensure that they all work in the most efficient and effective manner.

But we've all been trained as engineers, designers, etc. We've not been trained to manage processes and people. Okay, we can overcome that in the same way that we overcome most things in business and that's by using the experience and expertise that we've gathered, and by using the experience and expertise of others to address the issue in the best manner.

However, if we don't take the time to step back and look at our businesses from this perspective, if we continue to work in the business as designers, engineers or whatever, instead of working on it as managers, then our expertise and experience is one-dimensional and does nothing for the overall efficiency and effectiveness.

Here's what you have to do:

- Have a plan for your business: a map so you know where you're trying to go. We've already stressed the need for financial forecasts. You can't really have one without the other.
- Identify the key information that you need to run your business and put in place a means by which you can readily extract this. It could be financial (cash received, profit, etc.), it could be process-based (units produced, wastage, etc.), it could be customer-focused (number of new customers, average spend, number of complaints, etc.).

  It probably should be a mixture of all three. Whatever the fundamental information you need to best measure the current performance of your business, you must have it to hand.
- Allocate a specific half day or day every month when you focus on the management of your business and nothing else. Put it in your diary every month for the year ahead and have it cast in stone. Get away from the office or lock your door, turn off your mobile phone and disconnect your laptop.

  Allow nothing to distract you from focusing on your business. Have a fixed agenda, have your key information available, and as a minimum, cover:

    - Finance (cash flow and profit)
    - Sales and Marketing
    - Workflow management
    - Staff performance and development
    - Customers' issues

  Nobody is expecting you to be Sir Alan Sugar. It's a matter of creating a moment each month when your mind is focused solely on running your business. Then you can return to the fire-fight knowing what the bigger picture looks like.
- Actively manage your team. Fans of "Hill Street Blues", the brilliant American cop series of the 90s, will remember the routine at the start of every shift when the sergeant would gather the watch together, run through everyone's duties, give out the messages and then finish in fatherly tones with, "Hey, let's be careful out there".

  This is what you need to do with your team, every Monday morning. Make sure everyone is informed, coordinated and up for the fight.

- Plan your work. The temptation is always to get on with the job but 5 minutes of planning saves hours of wasted work and pounds of lost profit. Make sure you record it too, as a point of reference.
- Review your processes. Firstly, because you shouldn't assume that the way you think things are being done is actually the way they are being done. Secondly, because the fact that something has always been done that way isn't a reason why it's the best way to do it in the future.
- Always be commercial. Of course you want to do the best possible job for your customers but look at the task from your perspective as well. Where could this go wrong? How could we lose money? Most importantly, how do we go about the job and its paperwork so that we cover these risks?
- Have a plan for continually training and developing your staff. It you simply continue to do what you've always done, and if your training is restricted to the internal passing on of knowledge, then the lack of ideas from outside is going to see your skills level gradually deteriorate. You and your team need to get out there see what's happening in the rest of the world, learn new skills and keep on progressing.

Let's summarise what we are saying here.

If you want to increase your profits, then the historical equation has been simple, at least in theory:

- Increase your sales by selling more often to more people at a higher price.
- Reduce your overheads by cutting costs.

Our argument is that this is too simplistic and potentially damaging.

Profit is an outcome of all the functions of a business. To improve it, you are therefore looking to improve a series of linked processes. Understanding the links and ensuring consistent actions is much more important. The way to increase your profit is therefore:

- Improve the effectiveness of your sales and marketing strategy.
- Improve the return on what you spend your budget on, getting more value per pound spent in all areas.

Manage your business more effectively. Perhaps, an old cliche but too important to ignore… <u>Work on it, not in it.</u>

Key summary action points

1. Re-read this eBook to fully understand the link between effective management and profit.
2. Understand that profit is an outcome and not a section of your business to be viewed in isolation.
3. Greater efficiency and smarter management = more profit

Wayne Searle FCA

About …

Many small business owners are either time poor, cash strapped or stressed out of their mind – perhaps all 3. As a small business owner myself, I know, at times I have felt this way.

If this describes your relationship with your business, I don't have a magic wand to make it go away instantly but I can promise you that the team at ESP will provide you with the support, advice and insight to make things a bit better and help you to start moving your business towards what you want it to be.

We start with caring deeply about our clients. You will come across plenty of accountants but you will need to go a very long way to find a bunch who care more than us. Frankly, we give a damn about you, your business and your family.

Are you any good at getting stuff done? Who gives you a kick up the backside when you don't? Our coaching programmes are designed to provide the accountability to help you take action.

We could sum all this up as…

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