

THE DONALD COOPER CORPORATION

Speaking and coaching internationally on management, marketing, and profitability



Management tool #B-5:©

Cooper's 'backwards' approach to profitability:

Introduction: In most businesses, the approach to profitability is, *"We'll do our best all year long and hope that there's a decent profit at the end of the year."* This 'do our best and hope for the best' approach makes no sense. So, below is my 'backwards' approach to profitability which is much more effective.

First, we need to know how much profit the business must generate to support the life we want now and in the future; to attract and keep a top-performing team; to give us a decent return on our investment; to finance the growth of the business and provide a cushion for bad times. Then, we need to determine what needs changing or fixing to make that bottom line happen....and who will do those things, by when?

As owners of the business, it should pay us, first, a salary equal to what we could earn working someplace else. Second, it should generate a return on our investment (ROI) of at least 12%** (15% - 18% is better) and thirdly, at some point we should own the space that we occupy in a separate Real Estate Holding Company. Our business then pays our Real Estate Company rent each month.

**** Note:** The term 'ROI' refers to 'Return On Investment'. How do you calculate your investment in the business? For all decision-making purposes, your current investment in the business is what you could sell it for next month. Nothing else matters. If you put \$1 mil into the business and could sell it for only \$600,000, you've peed away \$400,000.

You may need your Accountant's help with the calculations below.

A) What after-tax profit must the business generate to compensate us for our effort?

- a) To live the life we want\$_____.
- b) To save for the kid's education and our retirement.....\$_____.
- c) To pay off any personal debt that we have\$_____.
- d) And to\$_____.

TOTAL.....\$_____.

B) What after-tax profit must we generate to attract and pay top talent.....\$_____.

C) What after-tax profit must we generate to give us, as investors, a decent return on our investment (i.e. 10% or more)?

To generate an ROI of ____%, we must generate an after-tax profit of.....\$_____.

D) To generate enough profit to pay off debt, reinvest in the business to finance growth, to create a 'cash cushion' to get us through tough times, we must generate an additional profit of.....\$_____.

E) So, we need an after-tax profit of the total of **A, B, C & D above =**

\$

Another approach to calculating the profitability we need:

If we plan to sell the business by a specific time, the following will be an effective way to calculate the profitability we need to get the price we want.

- a) We want to sell the business in ___ years for at least \$_____ to live the life we want.
 - b) Businesses like ours, in our industry, typically sell for ___ to ___ times annual profit.
 - c) So, by the year _____ we must generate a sustainable profit of at least \$_____.
1. The total after-tax profit we must generate (item D on Page 1, or c) above...\$_____.
 2. Our annual after-tax profit for the most recent year (20__ __) was.....\$_____.
 3. The additional after-tax profit we must generate is (item 1 minus item 2).....\$_____.
 4. **What must we fix, create, start or stop doing to generate the bottom line we need and to create a sustainable business that, at some point, will prosper without the current owners?** Improving our bottom line and creating a sustainable business will come from specific decisions and actions, well executed. Below are 20 questions to get us thinking about those decisions and actions.

Next Steps: What needs doing or fixing?

- a) Is the market area we currently serve big enough to deliver the sales and profit we require? If not, how can we expand our market, redefine our market...or move to a more viable market?
- b) Is our business model (the basic operating premise of our business) viable? If not, how might it have to change?
- c) Are we the 'wise choice' for our target customers? How can we improve our product or service offering to be that 'wise choice'? What can we become 'famous' for? 'Famous' is good!
- d) How can we advertise and promote our value proposition more effectively? Advertising is creative bragging. What are we doing that's worth bragging about? Does our advertising 'grab' our target customers, clearly differentiate us from our competitors, and make us famous?
- e) Word-of-mouth advertising from delighted customers is the most cost-effective and believable advertising. What can we do to WOW and delight every customer and turn them into 'fans'?
- f) We need to increase sales by \$_____. How can we sell more to existing customers? Do all of our existing customers know all the ways we can be helpful? Are there products or services that we could easily add in order to sell more to those customers who already know us and trust us? Increasing sales by a little as 5% can make a huge difference on our bottom line, if we don't cut prices or spend big money on advertising.
- g) How might we attract new customers? What value message, that we can actually deliver, will 'grab' them? Who are the specific new customers that would have the biggest impact on our bottom line? Who will call on them...by when?
- h) Are there customers or products that are costing us money and need to be dealt with? Who are those customers? What will we do to make them profitable, or 'fire' them? What products are hurting our bottom line? How do we make them more profitable...or how do we drop them?

- i) Is our website world-class and current? Does it offer valuable information? Is it engaging? Does it have video? How can we drive more traffic to it? Who can help us with that?
- j) Do we have a customer / client database, and do we use it consistently to add value, build relationships and promote our business?
- k) Social media can be a powerful tool. How might we use it to engage target customers, build 'communities', add value and increase our sales? Who can help us with that?
- l) Are we price-competitive? Are we too expensive...or selling too cheaply? Raising prices just a little can have a huge impact on our bottom line.
- m) Do we make promises that we don't keep? What are they? How will we fix that? We cannot build a business on broken promises.
- n) Do we have policies that tick customers off? What are they, and how can they be fixed or eliminated? How could we turn our policies around to create a marketing advantage?
- o) Do we have enough staff? Do we have the right staff in each department? Are they properly trained? Are they delivering the customer experience that we promise and the operational efficiency that we need? Are they paid appropriately and fairly? How is performance measured, acknowledged and rewarded. How is non-performance dealt with? What needs fixing?
- p) How must we strengthen, develop and empower our management team so that they can, at some point, operate and grow the business without us.
- q) Do our premises need updating or rethinking in any way? Do we look 'new and alive' or 'old and tired'? Are we efficiently laid out? Do we look and feel welcoming? How we look and 'feel' matters to our customers and to our team. What needs fixing? Who will be responsible for this?
- r) In what areas of the business can we operate more efficiently by upgrading equipment, or by improving methods, processes or systems? Who will be responsible for this? Are there technologies that we need to embrace in the areas of customer service, proactive marketing, operations or logistics that will make us more profitable?
- s) What are our 15 largest expense items? How can we reduce each of them by at least 5%?
- t) When is the last time we asked each employee for their thoughts on how we can serve our customers better, operate more effectively, and create a more engaging workplace? Our staff knows stuff and they hate it when we don't ask. When will we do this...and who will be responsible for making it happen? It should be a quarterly or semi-annual event.

So, using these 20 questions to trigger our creative thinking and commitment to improve our bottom line, what specific activities, changes and initiatives will we commit to? For each specific activity, change and initiative document what will be done, by whom, by when, at what cost, measured how and rewarded how...and followed up by whom...when?

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