HOW TO

FREE GUIDE SERIES

Generate sales from fresh air

Sales increasing strategy

No cost revenue generation

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As a small business owner, you are in business for one reason: to make money.

Of course, there are other reasons you started or purchased your company. You may love the product you sell, or service you provide. You may love the challenge of turning a floundering company into an overnight success. You may just love being your own boss.

Naturally, this all means nothing if you are not generating enough income to support yourself and your family, as well as the people who work for you.

Nearly all businesses make money. Unless not a single product or service is sold, there is always money coming in. But there is also always money going out. Supplies, wages, marketing, acquisitions and operations all contribute to the expense of just staying in business.

Simply put, profit is the difference between money in and money out. This is the dollar value of your sales, minus the cost of those sales.

In business, you will find that everyone wants to make more money. They want to increase their sales, get more money coming in. **What often gets overlooked is that the true secret to making more money is not increasing sales but increasing profit.**

What is Profit?

Before you can take steps to increase the profitability of your business, you have to have a solid understanding of:

- types of profit
- what factors influence profit
- what your profit is *right now*

Types of Profit

There are two main types of profit:

Gross Profit

Gross profit is the simplest form of calculating profit. It is simply the money that comes through the cash register, minus the cost of acquiring or providing the products or services.

The formula is:

Total revenue (sales) – cost of goods or services sold = Gross Profit

Net Profit

Net profit is a more accurate reflection of your income. It is calculated by taking your gross profit minus expenses over a specific time period (usually by quarter).

The formula is:

Gross profit – expenses (cost of running a business) = Net Profit

Factors that Influence Profit

Profit is your bottom line. It is the number that falls out the bottom when all other costs and expenses have been taken into consideration. Do you know what contributes to the amount of profit your business ends up with?

There are three main factors that influence profit:

Sales – Your Conversion Rate

The first, and most obvious, factor is the money that comes in the door through sales. In theory, the more sales you make, the more money you bring in, the greater your profits.

The ratio of potential customers to sales is called your conversion rate. This is the percentage of customers you have converted from leads to sales. So, a high conversion rate means more sales, and more money coming in the door.

In addition to your conversion rate is the lifetime value of your clients. It costs much less to convince a customer to make repeat purchases than it does to acquire new clients.

Costs – Your Product/Service Margins

The second factor is the cost of your offering – what your product or service costs you to acquire or provide. If you sell a product, this is the wholesale price you pay for the product. If you offer a service, it is the cost of your (or your employee's) time plus any materials used.

Your margin is the difference between the price you pay and the price your customers pay. If you buy toothpaste for $1 from the wholesaler, and you sell it for $3, your margin is $2. If a haircut costs $20 in materials and service, and the customer pays $50, your margin is $30.

Expenses – The Cost of Doing Business

The final factor is the cost of running your business – those not directly related to the specific product or service you offer. Expenses include:

- Office or store lease

- Computer equipment lease

- Employee salaries

- Utilities

- Marketing + advertising

Your Profit

It only makes sense that you need to know where you are to determine how to get to where you want to be. This applies to any plan to create in business.

Before you can increase your profits, you need to have an understanding of where your profits are currently – and if you're making any at all. The next section will take you through a process to review the specific factors that affect your business's profitability, and ultimately determine how much profit you are currently bringing in.

Taking Stock of Your Profits

Before you devise a strategy to increase your profits, you need to take a good long look at the money your business brings in, and the money you spend to run your business. You may wish to sit down with your accountant or bookkeeper to analyse the financial information that is available to you.

Decide on a specific time period to review – one that makes sense to your business, and one that will give you the most realistic picture of your business performance.

This will depend on if your operation is cyclical, or remains steady throughout the year. Usually, the previous quarter or the previous four quarters will give you enough of an indication.

Here is a general of items to review:

- Total revenue
- Total cost of goods or services
- Total cost of operations (overhead), including:
- Employee wages
- Recruitment
- Business development
- Utilities
- Rent or mortgage
- Office supplies
- Computer leases
- Incidentals
- Total cost of marketing campaigns

Total profit after costs and expenses for this time period: ____________________.

The Five Factors that Eat Your Profits

It is easy for business owners to compare their organizations to the apparent success of their competitors. Joe's Pizza may always be teaming with customers and appear to be making money hand over fist, while your pizza shop may have slower, but more steady business.

It is important to remember that a business with extraordinary sales figures is not necessarily a profitable one. Sales are just one element of your profit calculation.

Here are some other elements to think about when reviewing the profitability of your business:

Impulse Spending

How often do you make purchases for your business operations?

I'm not talking about acquiring new goods and services, but upgrading computers, taking your team out for lunch, or leasing a new colour photocopier.

Do you allow your staff to make purchases on your behalf? Who reviews these decisions? Take a look not only at *what* you buy, but *how* spending is structured in your company.

Small Margins

As we discussed in the previous section, your margins are the difference between your cost and the customer's cost to purchase your goods or services.

Typically, businesses that offer a variety of products will have both products with large margins, and products with small margins. The products with large margins generate the most income, so these are the products that staff should be focused on selling.

What many businesses overlook is that products with small margins will never generate a high level of income, no matter how many you sell. A store stocked with small margin items will never be able to increase their profit because they have so little margin to work with.

Your Customers

This may seem like a backwards way of thinking. Your customers spend money, so they are a positive factor in your profit calculation, right?

This is true for most of your customers. But remember the 80/20 rule of business – 80% of your revenue comes from 20% of your customers. These are your top 20%, or ideal customers. What about your bottom 20%? The group of clients who ask for the moon and never stop complaining.

These clients can be a huge drain on both your staff resources and your financial resources. Their true value to your business is minimal – they cost more than they bring in. Fire them!

Loan Interest

How many business loans do you currently have? Credit card debit? Overdraft? The interest you pay on these loans can be a substantial monthly cost to your business.

A loan from a bank is just like any other product. You can shop around for the best deal. Consider consolidating or restructuring your debit to minimize interest payments. Plan to search around for the best rate on a regular basis – every few months or quarter.

Vendors

Do you purchase your goods and services from a wholesaler or retailer? How long have you been in business with this company? What do you pay for goods and services relative to your competitors?

Ensure that you are dealing with as direct a vendor as possible to minimize your acquisition costs and increase your margins. If you have been doing business with a particular vendor for an extended period of time, consider renegotiating your business arrangement.

The Basics of Increasing Profit

Your Profitability Goal

Now that you have an understanding of the current profitability of your company, it is time to look at ways to increase your bottom line.

Like all other aspects of your business development, you need to have a clear idea of your intention or purpose before you begin any activity. Assuming you wish to increase the profitability of your business, you need to determine by how much and within what time frame.

Create a profit-related goal for your business, and write it here:

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Three Ways to Increase Profit

There are countless strategies for increasing profit, but ultimately you can only increase profit in one of three ways:

1. Get More Customers

Use marketing outreach strategies to generate more leads and convert those leads into more customers. Introduce a new offer, expand your target audience, or approach a new target audience.

2. Get Your Customers to Buy More Often

Use customer loyalty and retention strategies to get your existing customers to buy from you more often. Make it easy for them to come back and do business with you.

You can do this by adding value to your product or service, keeping in touch on a regular basis, and giving your customers incentive to make repeat purchases. Customer service is also an overlooked component of building a repeat client base.

3. Increase How Much Your Customers Buy

You'll naturally increase your sales when you increase the number of customers and how often they purchase. The final way you can impact your profit is by increasing the average dollar value of each sale.

This can be achieved by up-selling every customer, creating package offers, and finding ways to increase the perceived value of your offering to justify increasing the price.

Managing Costs

One important way to impact the profitability of your business is through cost or spending management. Controlling how much money goes out will help you ensure that a more money stays in your bank account.

Remember, however, that cutting costs can only help increase your profits so much. There is a point where you will no longer be able to reduce expenses, and you will have to focus on increasing sales.

Why Cut Costs?

Cost management may seem like an obvious way of maintaining a healthy business, but it is also one of the primary reasons 80% of small businesses fail. Overspending is a huge problem for most businesses – and they don’t even realize it.

Reducing costs is a great short-term strategy to boost profits. As I mentioned above, there is a limited amount of impact cost management can have on the bottom line, so it is an ineffective long-term strategy.

Cost management can also help you to generate more capital. A business that closely monitors and controls its spending is a much more desirable loan candidate than a business that spends freely.

Most importantly, this strategy will help keep your business profitable through high and low periods. It’s easy to spend money when your company is doing well, but this leaves little in the “just in case” account for downturns in the economy or unexpected expenses.

Where Can I Cut Costs?

Financing

As I mentioned, interest rates are a big culprit when it comes to eating profits. Take stock of how much money you are spending on a monthly basis in loan and interest payments.

Can this be reduced? Is there another bank that will offer you a lower rate? Is there a way to consolidate these loans into a single, low-interest account?

Alternatively, if your business is doing well and has a large amount of money sitting in the bank; consider investing it or placing it in a high-interest savings account. Let your money make you money instead of spending it on unnecessary business luxuries.

Suppliers or Vendors

Again, as mentioned above, make sure the price you pay for goods and services – for resale of internal use – is the lowest you can find. Try to deal directly with the manufacturer or distributor and renegotiate discounts and contracts with your vendors every year.

Hours of Operation

Evaluate the hours you are open for business each day, and why you have chosen the specific timeframe. Is it to compete with the competitors? Is it because you can serve the highest number of customers? Each hour you are open for business costs you money, so make sure you are operating under the most ideal timeframe.

Staffing, Wages, and Compensation

This can be a sensitive subject for any business owner or employee. It is important to look at staffing redundancies and capacity levels – as well as hiring needs – when evaluating cost management strategies.

Do you need to hire new staff, or can you build capacity within your existing employees? Is there another way to compensate staff, or provide performance incentives that are non-monetary, have a high perceived value, and inexpensive for your business? Remember to take time and care when implementing any changes in this area of cost management.

Place of Business

If you operate an office in a downtown metropolis, you are going to have substantially higher operating costs than a competitor who runs an office just outside the city limits.

Make sure you can justify your location, and the amount of money you spend to be there. Consider the following questions:

- Are my customers impacted by where I do business?
- Do my customers need to visit my office?
- What impression does my business need to present?
- Do I need parking facilities?
- Do I need to be visible?
- Do I have staff to employ?
- Am I near public transit, lunch outlets, and other amenities?
- Do I need access after business hours?
- Should I lease or buy?
- What other costs are specific to this location?

Eliminate the invisible!

What could you and your staff live without? What wouldn't you notice if it just disappeared one day? Take stock of expenses that are not being properly used or appreciated. Think of amenity-based items, or convenience costs, like:

- Gym Memberships
- Morning refreshments (muffins, donuts, etc.)
- Publication Subscriptions
- Designer coffee and tea
- Fancy collateral packaging

Your Pricing Strategy

The cost of your goods and services has a direct impact on the money you bring in. Your pricing strategy is so important to your business that can even determine your success.

Deciding how much to charge for your product or service is a challenging task. You need to factor in your own costs, the product or service's perceived value, and the going rate. Ultimately, you want to be able to charge as much as possible for each item, without overpricing yourself out business.

Avoid the Lowest Pricing Strategy

The days of the lowest price guarantee and pricing wars are over – especially for small businesses. The "big players" in the marketplace will quickly put you out of business if you try to compete on price. Their pockets are deeper, and they have lower operating costs due to their sheer size. They can afford to – you can't.

Clearly Position Your Company and Your Offering

How do you want your target market to view your business, and your products? Are you trying to create an image of high quality? High value? Reliable service? Make sure your pricing is consistent with the image you are trying to project. If you are operating a high-end spa – you're not competing with the budget nail salon down the street, so your prices should be considerably higher.

Have a Good Working Understanding of Your Margins

Know how much the product or service costs you to offer before you establish a price. Do these costs remain consistent, or do they fluctuate? Restaurants that offer high quality meat and seafood often price their meals at "market rates" as opposed to fixed rates. Calculate the fixed and variable costs associated with your product or service. You will want to work the cost of the product or service, a percentage of your overhead, and your own profit into the cost of each item.

Pay Attention to Factors Beyond Your Control

Be aware of any government or industry regulations on the price of your product or services. Some laws will actually limit how much you can charge for standard services.

For medical and dental services, most insurance companies will put a cap on how much a customer will be compensated for each service. Seek out all external factors that could impact your pricing.

Price with a Purpose

Your pricing strategy should be purpose focused. What exactly are you trying to do by setting your prices at certain levels? Here are some potential reasons for pricing strategies:

- Short-term profit increase
- Long-term profit increase
- Customer generation
- Product positioning
- Revenue maximization
- Increase margins
- Market differentiation
- Survival

Pricing Strategies

Cost Plus Pricing

This is the most basic pricing strategy. Set your price at a number that includes:

- Cost of goods or services, based on a specific sales volume
- Percentage of expenses
- Profit margin (markup)

Target ROI Pricing

Set your price at a rate that will achieve a specific Return on Investment target. If you need to make $20,000 from 1,000 units – or $20 per unit – then set your price at $20 more than cost, plus expenses.

Value Based Pricing

This can be a bit of an arbitrary pricing strategy, but it can also be the most profitable. Set your price based on the value or added benefit it brings to a customer. For example, if your product only costs you $40 to produce, but will save the customer $2,000 per year in energy costs, a price of $150 or $200 would not appear to be unreasonable in the eyes of the customer.

Psychological Pricing

What messages are you trying to send the customer when they're looking at your prices for your products? Do you offer the best deal? The highest value? These are reasons to choose prices that are higher or lower than the competition.

Pricing Guidelines

Price higher than cost. This may seem obvious but ensure that your pricing not only covers your costs, but potential fluctuations in sales volume and in the marketplace. If you sell half of your order, will you still make a profit?

Include expenses. If you price to cover your costs, will you also be able to cover your expenses and still see a profit? Your margin needs to pay for your expenses, leave you with something to live on, plus some working capital for the company.

Consider the 'fair' price. What do your consumers think is 'fair' for each service or product? This is impacted by your competitor's price, your company's image (high quality or high value, low cost), and the perceived value of your product or service.

Strategies to Increase Profit

Once you have a concrete understanding of where your business stands today in terms of profitability, minimized your operating costs, and restructured your pricing strategy, you can focus on other strategies to increase profit.

There are countless strategies and tactics that will help you to bring in more customers, get those customers to come back, and get those customers to spend more when they do.

Here is a list of ideas, many of which are covered in detail in other sections of this program:

- Advertise
- Establish an online presence
- Sell more high margin items
- Generate more leads
- Focus on referral business
- Increase customer loyalty and repeat business
- Increase conversion rates
- Restructure your team
- Reinvent your product
- Sell your intellectual capital