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Five Thing$ to Boo$t Profit$ Overnight PART TWO

As discussed in my article in the last issue of *ID&OI* magazine, Volume 46, Issue 5, page 34, there are five ways to increase your profits nearly overnight. Let's review.

1. Raise Your Prices
2. **Reduce Your Cost of Sales**
3. Change Your Product Mix
4. Increase Sales Quotas
5. Eliminate Crappy Customers

In the last issue we considered #1 on my list, raising your prices. I hope you did that as soon as you finished reading the article! Now let's consider #2 on the list, reducing your cost do sales.

Before we discuss how, we first need to clearly define cost of sales. Since a company's gross profit margin is the single largest influence on the bottom line, it's critically important to guide and control it's cost of sales. Typically for garage door dealerships, cost of sales is the material cost, tax, freight, direct and/or sub-labor plus any other costs directly related to performing the work such as equipment rental. Here's an example.

	Amount	% of Sales
Sales (Revenue)	$1,000,000	100.0%
Material Cost	$450,000	45.0%
Tax	$50,000	5.0%
Freight	$50,000	5.0%
Direct / Sub Labor	$120,000	12.0%
Other Direct Job Costs	$10,500	1.5%
Total Cost of Sales	$680,500	68.5%
Gross Profit Margin	$319,500	32.0%

Figure A

There are only two ways to increase gross profit margin. One way is to increase sales and the other is to decrease cost of sales. From the example above there are five components that make up cost of sales. By far the largest of these, which you have the most direct control over, are material and direct labor costs. Freight is also an area to consider but does not have as much impact. Tax is non-negotiable and Other Direct Job Costs in our example is a small part of the overall cost. So if we want to work at reducing cost of sales the largest possible impact is with material and labor cost.

Material Cost

Big Ticket Items – What makes up our material cost? While we tend to first focus on new doors and openers, when we think about it there's a lot more to consider. There are the parts and accessories needed to install garage doors such as trim, angle iron, low voltage wire, fasteners, etc. Stocking parts for performing garage door service is also a big area of cost and can be a challenge to manage. While all of these should be monitored regularly, the area that can present the quickest and largest reduction of material cost is new doors and openers since they make up the bulk of a dealer's purchases.

Do Your Homework – My manufacturer friends in the industry will not like this next part. However you owe it to your company's profitability to analyze what your major suppliers are charging you for the products you sell. That will require you to spend a fair amount of time doing product cost research in order to see how your costs compare. Just as your local area has a market price for selling your products, it also has a market cost for purchasing. To do this you will need to entertain price quotes from competing manufacturers. I know this is not popular with your incumbent suppliers, but there's really no other way to gather viable data.

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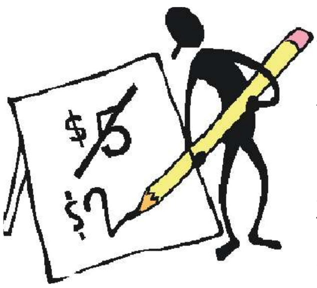
Negotiate – Once you have a good grasp on market cost and if you discover you are paying higher prices for doors and openers that meet the same specifications, I would urge you to sit down with your current supplier rather than just jumping ship. In most cases, the goal will be to continue buying from your same supplier if possible and in the process strengthen the supplier-purchaser relationship through open and honest negotiation. Having documentation to support the data gathered is extremely important.



Consolidate – Inevitably the volume being purchased will have some influence on your cost. Are you fragmenting your purchases between a variety of suppliers? If so, you may not be getting the deal you think you are. There may be some instant cost savings through consolidating these with a single supplier. This may also help with lowering your freight cost. While it would be nice to have the freedom to cherry pick the best from a large variety of suppliers, you will find that practice inefficient and usually will not yield the lowest cost. Plus it is difficult on your staff. Supporting multiple shipments, price structures, purchasing procedures and being sales experts on wide variety of manufacturers' products is a very tall order for most dealerships.

Another way to buy at a lower price point would be to increase the amount of purchased and decrease the frequency of shipments. Whenever possible, ask for special price concessions if your next delivery fills the truck (or even the majority of it). The manufacturer realizes a cost savings by not having to make multiple drops and there is no reason you should not share in this cost reduction. If not in a single shipment, perhaps you can lock in on a reduced cost for a series of deliveries over a finite period of months.

Price Per Project – Asking for special price concessions on a per project basis has been a long time practice in the garage door industry, mostly for commercial bid and larger residential tract building projects. But since entering the Great Recession beginning in 2008, smaller home building projects also qualify. Do not be bashful about going to your manufacturer with smaller projects, especially when those involve higher end products or securing new customers. When you do this make sure you have a written description of the project from the builder / developer that describes its overall scope and a time table projections for construction. You then need to extrapolate this data and present the potential additional sales this project would add to your purchases from the manufacturer. Remember the definition of a good deal is where everyone makes out.....the builder gets more competitive prices, you guard your margins and the supplier gets more volume from your area of the country. Everybody wins!

Prompt Payment Pays – A quick way to save instant cash is to take advantage of prompt payment discounts. In our example above, if the suppliers offered a 2% discount if paid in 10 days, there would be a $9,000 savings right off of the top. You can see that this would have a pretty dramatic impact on your bottom line. So if your suppliers offer discount payment terms, take them. If they do not offer discount terms, ask for them anyway. As they say, cash is king and speeding up the payment process is worth money to any business. For additional cost savings, consider paying with a credit card that gives you cash rebates. The hidden bonus in this scenario is by taking advantage of prompt payment discounts you are also building a terrific credit rating. Now who can argue with that?

Yes, massaging hard costs is a necessity in the monitoring and managing of your cost of sales. It is most likely an exercise of a combination of the points addressed above, getting better purchase prices, lowering freight, prompt pay discounts etc. This is most effective while holding or even slightly increasing your selling prices. The name of the game is maximizing gross margin and lowering your material cost is one big way to accomplish this.

Labor & Equipment

Hourly or Piecework? Ah yes, the old industry question, do you pay field personnel on an hourly or a piecework basis? Which is more cost effective? What are the drawbacks to each? We could devote another entire magazine article on this subject but for this discussion we will focus on how each can influence the direct labor component of your cost of sales.

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Productivity is the Key – Regardless of how field techs are compensated, the key to reducing your direct labor costs as a percentage of sales is by getting more productivity from each truck. This starts with setting definite production goals for each tech and holding them accountable by closely monitoring their progress every week. You can use dollars, units or whatever system you choose. Post the numbers in your service department so they can see where they stand each week versus budget. There may even develop some friendly competition among techs in the process to see who can be the most productive. A critical component of maximizing productivity is scheduling. Make sure that each truck has a full days work and is routed in a way to minimize "windshield time". Technology can help with this but nothing will take the place of someone managing the workload in a way that allows the tech to accomplish a full days production each day. Just by virtue of you and your team paying closer attention to production I can assure you that your company's productivity will improve. When it does, remember to celebrate with your team. Pizza parties, gift cards or small bonuses, whatever....just celebrate the victories and in the process reinforce the behavior you want to replicate.

Piecework Works – I have always been an advocate for compensating residential installation techs using a piecework method. It's an easy way to control labor cost and fosters an attitude of pay for performance. The tech sees a clear way to make more money simply by becoming more productive. The more you do, the more you make. I would urge you to review your piecework rates often. Rates should be consistent but can vary between products. Consider a higher piecework installation rate for custom carriage doors versus a lower rate for builder grade pan style garage doors. Of course quality has to be closely monitored and the tech held accountable for call backs related to his installation but in general, piecework works well when considering lowering your direct labor costs.

Making 8 – The main argument against paying techs on an hourly basis is the perceived tendency that they will fill the eight hour work day with whatever work is assigned with no urgency like piece workers. This is fondly referred to as "making 8". I would agree that this would be true IF there is no production standard in place with hourly techs held accountable for it. My companies found that tying quarterly or annual bonuses to production was a good way to avoid the "making 8" trap.

Overtime is a Killer – Usually jobs are estimated using normal hourly rates. Seldom does a project recover from a margin standpoint when the direct labor cost comes in at 1-1/2 times the originally quoted cost. Of course there are times when it is absolutely necessary and cannot be avoided but these should be the exception rather than the rule. Overtime should therefore be monitored in a hawk like manner and reserved for after hours emergency service or other situations where the customer is paying a premium. If you want to control your labor cost, put the tourniquet on your overtime and budget. Congratulations, you've just lowered your direct labor cost and increased your gross profit.

Add Ons – It's 3:00 PM and you hear from your installation tech that he's completed his job for the day. Send him home, right? Wrong. Check the dispatch board and see if there are service calls close to him that he can perform which will improve his productivity for the day and provide good customer service. A simple spring change could make the difference in having a good day to having a great day of production. While you may not be very popular with the tech at the moment he may have a different attitude come bonus time. Consider this example on an annualized basis. Let's say this same installation tech gets an extra service call just twice a week. The average ticket price per call is $225. This would add an amazing $23,400 of additional production (sales) per year. Highly profitable production to boot! Add "add ons" to your daily schedule and watch your margins improve.

Subs – If you use subcontractors you are in a good situation to control and often lower you direct labor costs. If they truly are subs and not glorified employees that you are calling subcontractors to avoid taxation and benefits, then they are independent businesses. As such negotiation is far easier than when they are regular employees. Rather than just pay what you've always paid, consider negotiating better labor rates based on the projects size and scope. Perhaps reduce installation work and increase repair projects. While you can value your subs' efforts, they have to be part of the negotiation process when it comes to controlling direct labor costs. When

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is the last time you reviewed what your subs are charging you? When is the last time you got other subs to quote?

Equipment – If you do a lot of heavy commercial and industrial work you are most certainly in the equipment business also. Either you own and maintain it, or you rent it. Either way the costs are significant. If you are not budgeting for its use on a per project basis it is costing you even more. For installation work, consider establishing an hourly or daily rate and plug this into your estimate before computing the project's bid price. For repair work, here's an idea....CHARGE FOR IT! If you have to break out an aerial lift in order to repair a large overhead door, the customer should pay at least the same if he had to rent it himself. So charge accordingly whenever possible. This will instantly pump up gross margins while decreasing other direct job costs as a percentage of sales.

Impact of Reducing Cost of Sales

So let's say you were able to do what I am suggesting relative to reducing your cost of sales while at the same time increasing your gross profit margin. Using the previous example (Fig. A) let's assume the following.

- You were able to get an overall reduction in material cost prices of 3% through better negotiating and prompt pay discounts.
- By reducing your material cost, you in turn reduced your tax on it.
- Since consolidating purchases you were able to reduce freight expenses by 2%.
- You instituted piecework and tightened up O.T. yielding a labor reduction of 1.75%.
- You began charging for equipment used for repair jobs and budgeting for it on installation work.

By making these reductions to your cost of sales here's what that same financial snapshot might look like (see Fig. B).

	Amount	% of Sales
Sales (Revenue)	$1,000,000	100.0%
Material Cost	$436,500	43.6%
Tax	$48,500	4.8%
Freight	$49,000	4.9%
Direct / Sub Labor	$117,900	11.8%
Other Direct Job Costs	$8,000	0.8%
Total Cost of Sales	$659,900	65.9%
Gross Profit Margin	$340,100	34.1%

Figure B

The results shown in Fig. B are definitely worth the effort. In our example, a dealer doing $1 million in sales dropped an additional $20,000 to the bottom line and improved his gross margin from 32% to 34%. All by effectively managing cost of sales more aggressively. Just imagine if this is done in concert with a slight price increase….a double dose to the bottom line!

Summation – The title of this series of articles suggests profits can be boosted overnight. While this sounds catchy it seldom works that way with a few exceptions. The fight to constantly improve profits is an ongoing battle that can be won. But it requires you, the owner, setting policy, monitoring its compliance and constantly looking for ways to sell more at a higher price while controlling costs. Is it easy? No way. Is it worth it? Definitely, or you would not be reading this article. My good friend and fellow contributor to this magazine, John Zoller, says "never in your business life will you ever be able to spend a whole dollar". He's telling us that while the sales number gets so much attention it's really in the percentages that we dig out our profits. Dropping a couple of points to the bottom line can make all the difference in your year.

Next issue we look at #3, boosting profits by changing your product mix.

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