

MAKE A FINANCIAL NEW YEAR'S RESOLUTION IN 2012

By: Gary J. Turnquist, CPA, Blanski Peter Kronlage & Zoch, P.A.

The continued pressures put on manufacturing companies resulting from an improving yet fragile economy, including: shortages in skilled employees, demands from major customers to reduce prices, demands to shorten lead times, and increasing operating costs such as health insurance are forcing company management to once again look at ways to make improvements in order to maintain or increase margins on products and services.

Some of the key areas to focus on are revenue, production efficiency, controllable costs, and discretionary costs.

Let's begin by looking at revenue. Your first reaction may be: "We can't increase our prices to increase revenue because we already are being asked to reduce prices and new business generation is very competitive."

This statement is true in most cases, but there are some things you can do and should consider looking at strategically. First of all let's examine pricing. You may not be able to adjust pricing on all products or services, but it's a good idea to explore the opportunity to increase pricing on value added services that are unique in nature or have a very high perceived value to your customer.

Secondly, examine the potential effect of a price increase. There are ways to calculate how much of a reduction in revenue you can absorb without reducing the amount of gross profit available to cover your operating expenses if you raise prices and consequently lose some business. You may be surprised to learn that you can absorb a loss of customers and not reduce profits. This coupled with analyzing and ranking your customers can lead to increased profits by also reducing expenses associated with activities that are not profitable. If you must reduce prices to keep a valuable customer, look for opportunities to get a larger portion of the market share in exchange for offering reduced pricing.

Also, make sure you look at all the add-on services you provide and see if you can identify some areas you are currently giving away to your customers where you may be able to charge a nominal amount. These new revenue areas may not be a lot individually, but in the grand scheme of things, may add up to

a valuable additional revenue source.

Production efficiency is an area to examine regularly for opportunities to improve gross margins. Areas to review include: material acquisition and handling expenses, production labor efficiency including non-production time, maintenance time, clean-up time, set-up time, and actual production run time, just to name a few. Improvements in this area will not only result in increased profitability for your company, but also will improve lead times, which may allow your company to accept projects it may be currently losing.

Controllable costs are expenditures that must be incurred, but can be controlled to a certain extent by the company. Examples of these types of costs include: production supplies, office supplies, waste handling, property and casualty insurance, and, believe it or not, labor and health insurance expenses. Many companies have significantly improved their profitability by analyzing expenses, identifying those that can be controlled, and focusing on reducing certain controllable expenses. This is an area that can significantly reduce your "costs of doing business" and can allow you to retain your significant valuable customers by reducing prices, yet maintaining the margins you need to cover your overhead expenses. Remember to look for opportunities to produce more products or get a larger piece of the market share of your major customers in exchange for reducing prices.

Discretionary costs are just that, discretionary. You should regularly review discretionary expenses to determine if they should continue to be incurred. Some of these types of expenses are "necessary" for morale, perception, etc. If you are focused on occasionally reviewing them, you may discover ways to accomplish the same goals for less.

By regularly reviewing controllable and discretionary expenses, you can reduce the chance of expenses creeping up over time and not being noticed. You will be surprised how often this happens and by how much expenses can gradually increase over a period of time.

There are many other areas companies can focus on to improve profitability and cash flow. The key to achieving the results you desire (and need) is to formally commit to and implement an action plan aimed at strategically improving identified areas. Also, an outside advisor/facilitator is an extremely valuable piece of the process, as that person can efficiently assist management in establishing the process, monitoring the time line, and providing accountability to ensure the plan is not only developed but is actually implemented.

MARK YOUR CALENDAR!

2012 Grand View Summit
Thursday, April 26, 2012
3:00 – 7:00 p.m.

Location:
Minnesota Children's Museum
10 West 7th Street
St. Paul, Minn. 55102

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