

3 False Assumptions Business Owners or Their Managers Make about their Products and Services

By Kelli Hoskins, Master Business Coach, ActionCOACH



'In order for an organization to make money, the value of the product (as perceived by the market) and the price charged has to be greater than the combination of the investment in inventory and the operational expense per unit that is sold,' Eli Goldratt, The Goal. Or more simply put, in order for your business to make money, each product or service you sell must make money.

Jim Collins refers to this as your 'Economic Denominator' in his book Good to Great. It sounds easy, like it should be obvious. Therefore every business owner or their managers must be doing it. If this were true, then every business owner who supplies a marketable product would be rolling in the dough. But they're not, so they don't.

Here are three false assumptions I see many business owners or their managers make:

1. We're making good money so we must already be doing this
2. It's ok that we don't make as much money on some of the products or services we sell because we make it up on others
3. If we could just get more customers or make more sales, we'd make more money

As a result of these false assumptions, I see one of four outcomes:

1. Cash is left on the table which slows or restricts business growth
2. The business remains a good business, yet rarely becomes a great business
3. The owners remain a slave to their business their entire life
4. The business / owner goes broke

The only way to know for sure if you are maximizing your 'Economic Denominator' is to measure it. So, how much do you measure? And, how much cash are you leaving on the table? The first step is to identify your 'Economic Denominator.' It could be per transaction, per customer, per employee, per service van, per square foot, per hour.

Let me give you an example from a real company I worked with in the auto repair business whose economic denominator is per direct labor hour – because the number of available direct labor hours drives their capacity and therefore their ability to make money:

	<u>Job A</u>	<u>Job B</u>
Revenue	\$3,900	\$9,000
Material Costs (33% Markup)	\$2,250	\$3,000
Labor Costs (100% Markup)	\$ 450	\$2,500
Direct Costs (COGS)	\$2,700	\$5,500
Gross Profit \$	\$1,200	\$3,500
Gross Profit %	30.8%	38.9%
# Labor Hours (@ \$25 Per Hour)	18	100
GP \$ Per Labor Hour	\$ 67	\$ 35
Direct Labor Hrs Per Month (10 Techs @ 40 Hrs @ 90% = 36 Hrs/Tech)	1560	1560
<u>Potential GP \$ Per Month</u>	<u>\$104,250</u>	<u>\$54,600</u>

Like this business owner, I bet you initially thought that Job B was the better job, and that you want as many Job B's as you can handle. This business owner and his managers also thought Job B was their most profitable type of job, yet they were leaving \$50,000 of cash on the table EVERY MONTH because they did not measure their profit per direct labor hour and they made false assumptions about the profitability of their products and services based on revenue, gross profit dollars and cash in the bank, and ignored their economic denominator.

The other mistake this business owner almost made was to move to a larger facility or to invest in the expansion of his current facility because he 'needed more sales to make more money,' believing the only way he could do more business and make more money was to increase the size of his facility, at **Massive Costs** based on **Massive False Assumptions**.

Every business has an 'Economic Denominator,' and every business owner who is not consistently measuring his profit per economic denominator is making false assumptions about the profitability of his products and services. Therefore, you are leaving money on the table which means you are destined for one of the four likely outcomes above.

[Order My FREE Economic Denominator Analysis Now!](#)

This month ONLY we are offering business owners the opportunity to:

- ✓ Learn how to **Measure your Economic Denominator for FREE**
- ✓ See where you are **Leaving Cash on the Table** in your business; and
- ✓ Learn the TOP 3 things you can do to **Increase Your Profit Per Economic Denominator NOW!**