SixthSense
BUSINESS

Business
is Simple

People make it complicated

Everything you need to be 'Commercially Aware'

By Dave Gammon

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FOREWORD

Internal Audit used to get a bum rap amongst the professions. The profession was viewed as a necessary evil for large companies and the place where failed accountants were dumped. Of course, some of this stigma rubbed off on me. Its was my professional home for over fifteen years of my career.

After I had worked in the Tesco Internal Audit Department for a few years, I applied for a job as a commercial buyer and interviewed well. The interviewer was really impressed with my knowledge of the business because I'd been around most aspects of it, but he didn't give me the job because he said I didn't demonstrate 'commercial awareness'.

Even after I had moved profession to Operations, the prior label of lack of commercial awareness plagued me. Eventually, after over twenty years of experience, I got the chance to do an MBA in what would be my last corporate role.

I started studying and was getting excellent grades but found it interminably dull. When we were asked to explore a case study in the development of Tesco, the realisation hit me. The study examined the company strategy when I worked there but bore no resemblance to the strategy we were following or what had really been going on - it was grade 'A' baloney!

Business is simple. It is only when you add people that it becomes complicated.

I wasn't aware of it at the time because I was held back by the labels and other mental baggage I was carrying. When I became a business coach working with small businesses, I realised that I had all the commercial awareness AND people awareness necessary to help these companies grow.

You can find everything you need to know about running a business in this small book.

It is my gift to those who need to be 'commercially aware' and, in particular, to those of you who don't think you are!

David A Gammon
LEADERSHIP COACH

1 The Timeless Truth About Business

Businesses exist to create a profit; to sell products and services for more than they cost to provide.

Companies do this by providing products and services using one of four business models.

RETAIL

The company buys products from suppliers, adds a profit margin, and sells them. They add value to customers by giving them convenient access to the quantities of products that customers want. Think retailers and wholesalers.

BUILD

The company buys raw materials and uses labour and assets to turn them into something that they can sell for more than the cost of making it. As a result, they add value by creating products that customers need/want in a more affordable or less time-consuming way than the customer doing it for themselves. Think manufacturers and construction companies.

SERVICE

The company provides people that have skills, time, and knowledge. The profit comes from charging more for their time than it costs to employ them. They add value by doing things that customers can't do for themselves in an economically sensible way. Think accountants, consultants, and contractors.

HIRE

The company owns an asset or assets. It sells the use of the asset and charges more than it costs to own and maintain it. They add value by giving customers access to, or use of, the asset that would be uneconomic or difficult to obtain otherwise. Think logistics, hospitality, and holiday companies.

A by-product of this value creation is that companies shape the lives of the customers they serve, the suppliers who serve them, the people and who work for them.

They also serve the communities in which they operate by creating wealth, employment, and taxes.

It looks like money, but it ain't money.

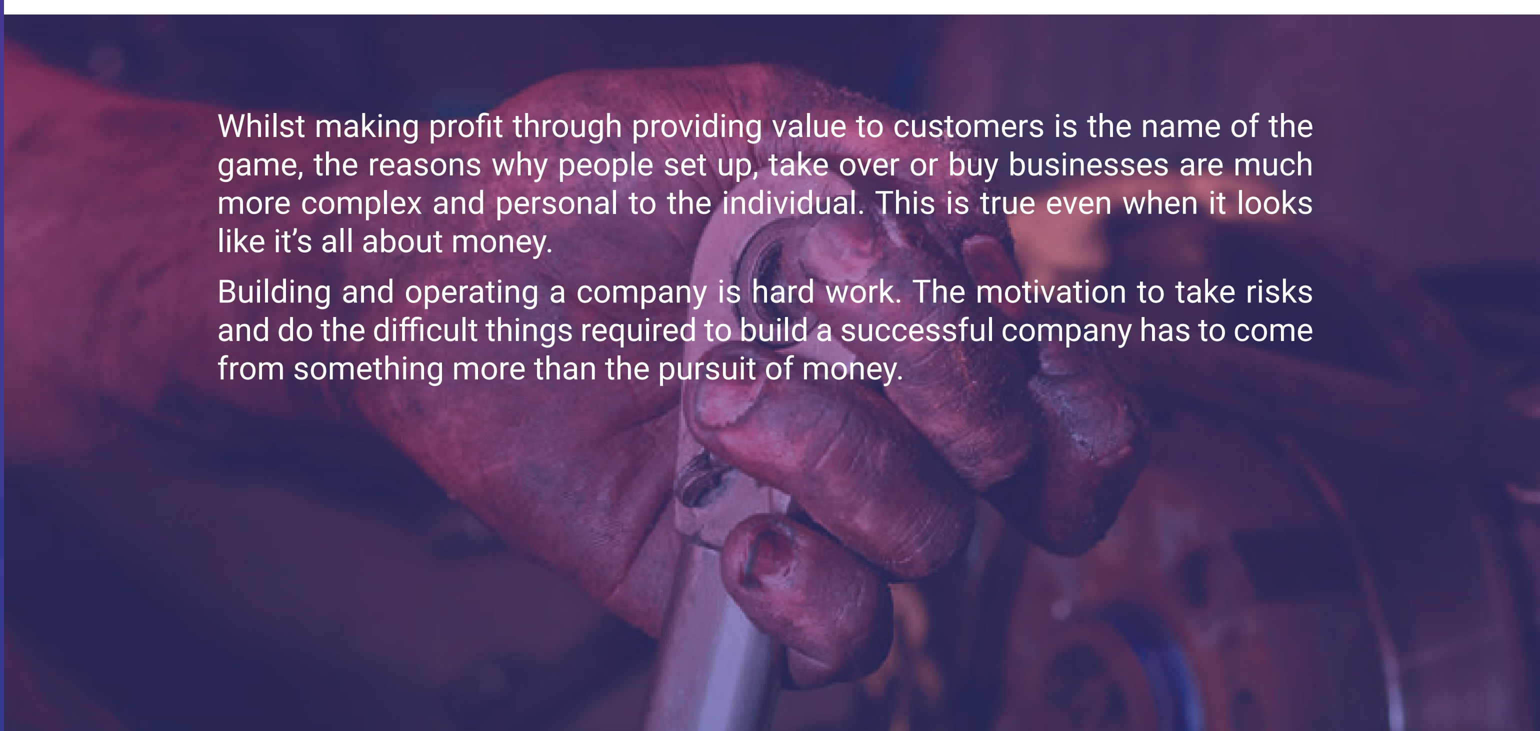
I had a fascinating conversation with a business owner in Basingstoke. When we met, he was building his third business in the I.T. industry; having already made and sold two eight-figure turnover companies.

He didn't need more money (he had a lavish lifestyle and didn't want for anything) and was not exactly passionate about the boxes of I.T. equipment he sold to customers.

I asked him the obvious question, "Why are you going to all this effort to build a third business (identical to the two he had already sold) if you don't need the money or have a particular passion for what your company does?"

It took a few asks of this question before we got to the truth. Even to him it looked like it was about money but I kept his feet to the fire until he gave me a better answer.

He became energised and animated as he described finding and kitting out the building, recruiting, training and the buzz of the company's first sales. The 'doing' of the company set up is what got his cylinders firing.



Whilst making profit through providing value to customers is the name of the game, the reasons why people set up, take over or buy businesses are much more complex and personal to the individual. This is true even when it looks like it's all about money.

Building and operating a company is hard work. The motivation to take risks and do the difficult things required to build a successful company has to come from something more than the pursuit of money.

2 Trade-Offs and Choices

“On an important decision, one rarely has 100% of the information needed for a good decision no matter how much one spends or how long one waits. And, if one waits too long, he has a different problem and has to start all over. This is the terrible dilemma of the hesitant decision maker”

Robert K. Greenleaf

Good commercial decisions require:

Informed guesswork as to what balance of margin, experience and quality will constitute value to their potential customers

Choices about where to apply limited resources (time, attention and money).

Decisions also have to be made in the face of complexity and uncertainty driven by the broader forces of technological, competitive economic, social and behavioural change.

We can never know what potential existed in the decisions we didn’t make. There can be no such thing as a perfectly commercial decision. They are guesses that are hopefully informed by clean perspectives and predictions.

But ultimately everything decision has to be made in the knowledge that it might not work.

Being comfortable with failure, experimentation, and low attachment to plans is a prerequisite for commercial success.

Squaring the Triangle - The Fundamental Trade-Off

I was sent a picture of a shop sign from the United States, which read as follows:

We do three grades of service. You can pick any two.

CHEAP, FAST and GOOD.

Many commercial decisions require a trade-off between product quality (good), customer service (fast), and margin (cheap).

It costs money to have good product availability, quality, and high levels of customer service.

If the customer demands cheap, fast AND good, something has to give[1].

The right balance between these three elements is a matter of choice made by leaders in the company.

For example, here in the U.K., we have several food retailers of which Aldi and Waitrose could be said to be at opposite ends of the trade-off choice.

If you visit these companies' stores, you will notice a difference (at least at a level of perception) in their approach to service, quality, and the pursuit of profit. All of them are successful, but each uses a different trade-off model.

Choices and Limited Resource

> **"More businesses choke on opportunity than starve of them"**
>
> *Verne Harnish*

Every company has limited management attention, financial firepower, assets, and space. So, choices must be made from an unlimited range of potential courses of action that will deliver the best return on the energy, time and money put in.

Any company can be judged by the level of return on investment, risk and energy it achieves.

This debate permeates every financial and priority decision.

For example, before investing in more people, equipment, stock, selling space, marketing, or anything else it might need, the business will want to be sure that spending that money will generate a return within a reasonable period (often called the PAYBACK PERIOD).

1. Unless the business can find a leveraged solution (e.g., a change reduces the cost of product quality or customer service).

The payback is not always measured financially.
The payback may come in the form of:

Scale
Growing market share and sales through expansion (new markets, new product/services or acquiring other companies).

Consistency
Achieving better consistency of experience for customers.

Optimisation
Improving gross and net margins.

Resilience
Reducing the risk of excessive reliance on particular markets, customers, products, staff members or assets.

Exit
Changing the owner's relationship to the business.

S C O R E

3 Uncertainty and Possibility

"Creative exploration is impossible without humble acknowledgement of the unknown"

Jordan Peterson

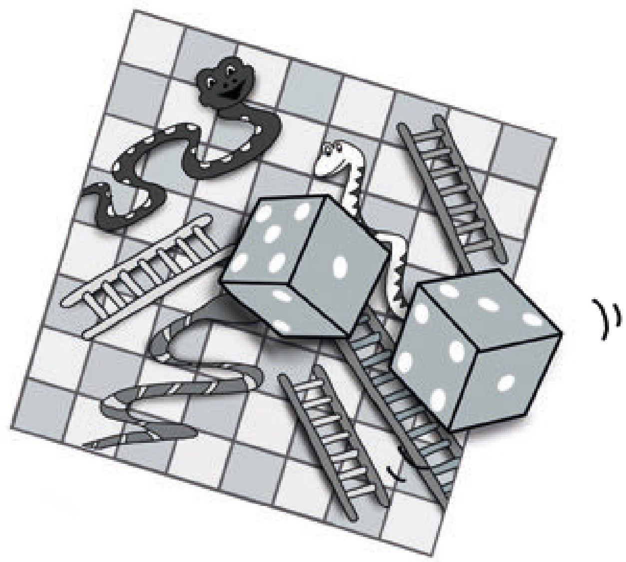
Being in business is like playing a game. The characteristics of a good game include:

a board, court or field of play and a set of rules;

a degree of uncertainty, unpredictability and adversity;

and an outcome that determines who wins and loses.

The Field of Play



In business, the field of play is the market(s) we operate within. The market dictates whether the way the company tries to play the game (its strategy) works or doesn't.

The market presents opportunities to move forward and challenges to overcome, many of which are outside our direct control.

Markets are constantly shifting[2] as economic, social, commercial, political, legislative, and technological forces reshape the field of play (the game's rules) and how it is possible to achieve results.

When I worked at Tesco in the late '80s, we could accurately predict the turnover of stores generating sales of more than £1m a week to within a few thousand pounds.

It's doubtful that level of precision is still possible in the food retail sector, given the level of constant change.

Companies must have their 'antennae up' and be tuned in to market shifts. They need to be willing and able to change strategies, plans and activities to exploit new opportunities and avoid commercial land mines.

2. Arguably faster than ever.

Unpredictability and Chaos

Good games introduce unpredictability and adversity by the uncontrollable actions of competitors, the throw of the dice and rewards or penalties applied under certain conditions.

Without them playing the game would be boring.

Business is loaded with uncertainty and adversity created by the need to continuously move forward in the face of changing customer behaviours, competitor actions and new technology.

Companies roll the dice (by making choices on what to spend money, time, energy, and when) in the face of uncertainty, embrace and deal with internal and external setbacks and keep playing until they have won the game[3].

The Outcome

The goal of most games is relatively straightforward; to beat everyone else who is playing or at least emerge intact at the end.

Companies seek to maximise the outcomes they attain for their efforts, but the owners define what it means to win the game.

It is often a compromise between individual and company results and an attempt to balance between several conflicting ideas:

If an intelligent computer ran a business, it would make all decisions using pure logic and probability. However, business leaders' deeply held values and beliefs, including loyalty and fairness, play a significant role in business decisions.

3. If you would have it any other way, then business is probably not for you.

4 Levers

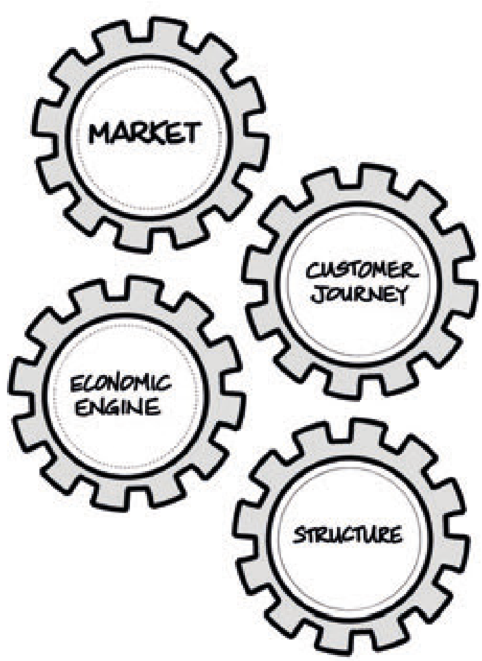
As an Auditor, I was sent to examine subsidiary companies, about which I knew very little. Then, in just four weeks, I had to review the entire operation and write a report to the Board about the extent to which the company was under control (or not). These reports were serious and sometimes career-defining for Auditees.

I had to be sure of my facts, and my review had to have depth and breadth as you could be sure they'd be looking for holes in my findings.

This seems like a lot to do from a base of no understanding. Luckily, I knew that there was a limited number of elements I had to understand to get under the bonnet of any company.

As a business coach, I refined and adapted this model over the years as a framework to examine commercial strategies, make decisions and raise commercial awareness.

The model looks like this:



Commercial awareness comes down to the consideration of four simple elements in any decision, idea or action.

The Four Elements

A company operates in a defined **market**. The company's position in the market and the market's perception of it determine its relevance, now and in the future.

Customers experience the company, from initial inquiries to their last interaction. This **customer journey** experience dictates how much value they create, and how long they stay.

A company has an **economic engine**, a set of numbers that determines its ability to survive, make a profit and grow.

Companies deliver customer experience and economic value through a **structure** of people, systems, assets, and data.

Well-rounded commercial ideas, strategies, plans and decisions come from a balanced and whole form consideration of these four things.

Let's look at each in turn.

5 Market

One of my clients owns three engineering companies. One of these distributes, designs, and builds solutions with an aluminium profiling system (he describes it as Meccano for adults).

The system has been used to build a vast range of products, including sports shelters, F1 wheel trolleys, airport conveyor systems, office desks, and a wide variety of engineering systems.

In discussion with the owner, we concluded that their enquiries were so diverse that defining a common target market was pointless.

One day he was asked to build some dugout shelters for a football club. He decided to create specific marketing campaigns to reach out to other customers in that target market. This was met with some success and brought in sales that would never have been found otherwise.

Every company operates within a market, but what comes first, the product/service or the market?

Customer-led company develops products or services to respond to customers' requests.

Product-led company develops products or services and then looks for markets and customers to sell them to.

It's not this binary for most companies and in reality, both are market-led approaches. Most companies adopt a blend of these product and market led approaches.

For example, a customer-led company develops products or services to meet specific customer demand. Still, it searches for other customers who may need the same product/service.

Conversely, a product-led company still use the feedback they get from customers to modify and adjust the product/service to maximise its commercial value and attractiveness.

Everyone or anyone is NOT a market

There isn't a product on the planet that everyone would need or want, at any specific point.

Products and services are designed and marketed to a specific customer or group of customers. This group is called the TARGET MARKET[1].

4. Or markets. There is no rule that says you can only have one target market.

The target market comprises customers that fit the profile of people or organisations most likely to use the company's products/services. These groupings may be:

- ***Geographical location***
- ***Technical needs and limitations***
- ***Demographic - age, sex, company turnover, wealth, number of employees***
- ***Psychographic – attitudes, beliefs and values***
- ***Lifestyle - interests, social groupings, preferences***
- ***Purchasing - purchasing behaviours and attitudes***

Companies may have customers from outside their target market, but marketing efforts should focus on the defined characteristics of their target customer.

The more precisely a target market is defined and understood the easier it is to market to[5] .

Companies can conduct MARKET RESEARCH to determine how many potential customers exist and what their preferences and behaviours are.

How big is your piece of the pie?

It is unlikely that any company is the only one offering products/services in a chosen target market[6] .

The size of a company's piece of its target market is its MARKET SHARE[7] . Understanding market share indicates how much growth potential exists in a target market.

A company would aspire to have total control (or at least a dominant proportion) of its target market. This would allow it to control supply, keep prices up and profits high.

In most markets, there is competition[8]. This requires companies to continually develop, market and evolve their products/services and reputation.

5. The market needs to be addressable for it to be commercially viable to reach and acquire customers.
6. and if it is, it won't be forever.
7. This is normally expressed as a percentage.
8. And often legal and regulatory mechanisms to prevent one company dominating a market.

Utility and Significance

While working for Tesco, my boss asked me to analyse the annual reports of the four biggest food retailers. This analysis was not financial, but rather the Board wanted to understand what companies were telling shareholders (or potential investors) about their operations and strategies.

All four companies explained in their annual report that they had the best people in the industry! So at least three of them were lying.

For a company to succeed, there must be a sufficient level of demand for the products/services they offer to sustain the company and provide the desired profit level.

Customers buy products/services to resolve an actual or perceived need. A product or service primarily needs to 'do what it says on the tin' and fulfil the purpose the customer expects.

For example:

- I will buy a toilet brush, so I don't have to use my hands to clean the toilet.
- A company will buy raw materials so that it can make products.
- Companies buy consultancy to give them strategies for growth or improvement.
- My fiancé will buy a pair of shoes because she doesn't have enough of them.

These basic needs are what shape the product's UTILITY.

Understanding what represents good utility is important but that is not enough on its own in competitive markets.

If every COMPANY sells the same product/service in the same way, a customer only has the price to differentiate between them. Ultimately this forces prices and profits down (unless they can find ways of reducing their operating costs).

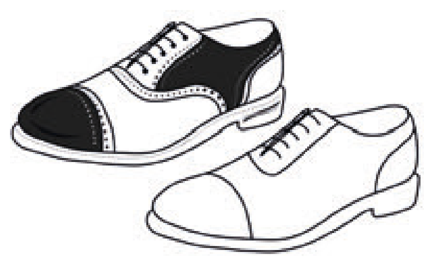
To overcome this companies, create points of difference that make their products/services more attractive than those of their competitors.

They try to create 'SIGNIFICANCE' in their products/services to set them apart from competitors.

Customers will pay a premium for a product/service if they perceive it has more value.

For example:

- I might pay a premium for a toilet brush that matches the colour of my bathroom.
- A company might pay more for raw materials that create less waste.
- Companies may choose a consultancy firm that has specific sector knowledge.
- My fiancé might spend more on shoes that have a Jimmy Choo label on them.



This is the differentiation that companies seek. It is often referred to as a Unique Selling Proposition (USP for short).

Significance is not just about design or features.

Customers may also make value judgments about the convenience of using a particular company, its reputation for service or quality, its cache as a brand (perceived status) or even the perceived safety of the decision[9] .

The value of a product or service is the customer's perception of its combined UTILITY and SIGNIFICANCE.

Nothing Lasts Forever

One of my clients was a hot tub retailer. The hot tub market first started to show significant growth in the U.K. during the '80s and accelerated sharply in the '90s attracting lots of new entrants into the market.

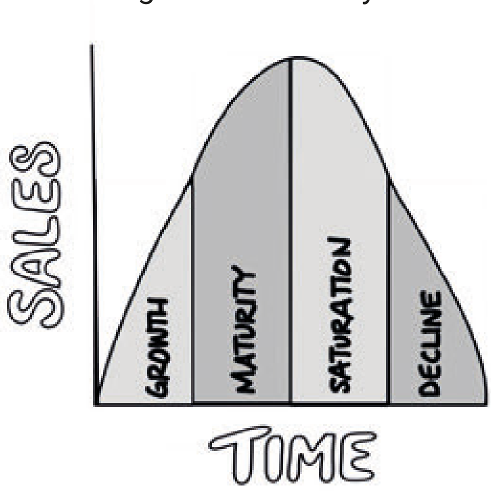
We had a discussion, prompted by a slowing of sales, about the point at which the market would reach saturation (when everyone who wants a hot tub has one).

After some research with their suppliers and a review of their own business position, we concluded that the point of market saturation was coming.

They subsequently decided to introduce swimming pools into their product range, a market that has not yet reached maturity in the U.K. They continue to sell the odd hot tub, but the swimming pool business has driven their company growth.

Even products and services that feel like they have been around forever will have undergone significant developments and changes over the years. Products/services must adapt to ever-changing consumer tastes, technological development, and competitor action.

All products/services have four stages in their lifecycle.



9. In the late '80s there was a famous saying in the IT industry; 'no one ever got fired for buying IBM'. This was because IBM were the oldest and most trusted name in the market, and it felt risky to buy such expensive and mission critical equipment from anyone else.

GROWTH

New products/services go through a growth phase as customer awareness and adoption grow. The growth phase can be sped up with pre-launch marketing (including crowdfunding approaches) or when the product/service is piggybacking on the pedigree of previously successful products or strong brand loyalty. If a product/service doesn't sell enough to make it profitable, it can be withdrawn.

MATURITY

A product/service eventually reaches widespread adoption in its market. This often attracts competitors into the fight. The need for marketing continues through maturity, and there are often changes to the branding and/or the product/service itself to keep it current and competitive.

SATURATION

Eventually, the market for a product/service reaches saturation. This is when no further new growth is possible due to the high percentage of customers who have purchased the product/service or a competitor's version of it. Growth is only possible through predation of competitors market share.

DECLINE

Sales of all products/services ultimately decline as alternative choices, changes in customer preferences or new technologies emerge.

The period over which products/services go through this lifecycle varies.

For example, Heinz Baked Beans have been in the maturity/saturation phase for many years, even though many copy products have also taken some market share. They continue to evolve the product with recipe changes, new packaging, branding modifications and even sub-brands.

On the other hand, the market for a new mobile device model can decline quickly due to constant technology evolutions and new model launches.

Companies that want to attract and retain loyal, valuable customers need to continually develop new products/services and continuously enhance and update existing ones.

6 The Customer Journey

To be sustainably profitable a company must attract, convert, and retain a sufficient level of customer sales.

The experience that potential customers (prospects) have of the company will determine whether they become customers or not. The company's ability to meet and exceed their needs will determine how long they stay and how much they spend.

This is the customer journey. Each customer has a unique experience of this journey.

Companies should define and continually refine this journey so that service and quality expectations are met (or exceeded), sales are maximised, and margins are protected.

The journey can be broken down into three phases.

ACQUIRE
The company attempts to attract customer interest and convert that interest into a sale. This is the domain of sales and marketing.

DELIVER
How the product/service is delivered to the customer. This phase is concerned with meeting the customer's expectations regarding quality and service while preserving the business margins. It is the domain of Operations and Customer Services.

KEEP AND GROW
How the company retains, and grows the value of, the customer. This focuses on deepening the understanding of the customer's needs, building the relationship, and finding the potential for further product/service sales. It is the domain of After-Sales, Customer Marketing and Account Management.

The goal of the customer journey is to create customer advocacy and referral.

Creating Interest

During the Second World War, carpet bombing was frequently used. This involved dropping many bombs on an area, hoping that a few of them hit valuable targets.

It was expensive in terms of resources (planes and bombs) and the potential for collateral damage.

In recent conflicts, precision weapons have emerged. These weapons reduce the risk of collateral damage and enable warfare to be waged at a lower cost and with lower collateral damage.

The more precisely you aim your marketing at specific customers, the better response rate you will get, and the lower your marketing cost per sale generated will be.

A company needs to make potential customers aware of its products/services. This process is often referred to as marketing.

Marketing involves a number of activities:

1. Identifying and matching products/services to markets.
2. Understanding the market and customer behaviours and needs.
3. Creating campaigns to attract the attention and interest of potential customers.
4. The design of branding, copy, advertising, packaging, online presence and printed materials to support awareness and interest.
5. Measurement of marketing return on investment.

Marketing campaigns are planned activities designed to raise awareness of the company and its products/services to generate new leads and customers[10]. There are two fundamental campaign types.

Push Marketing

Outbound campaigns that reach out to specifically identifiable prospects (people or organisations) in a target market. Examples include telemarketing, direct mail, and email marketing.

Pull Marketing

Pull campaigns seek to attract inbound inquiries or purchases by communicating information and value to create interest and desire in the minds of potential customers. Examples include online marketing, billboards and T.V. advertising.

The success of any campaign depends on three elements working together.

Target

The campaign can reach prospects with suitable characteristics through effective targeting.

10. Customer Marketing is a slightly separate discipline where campaigns are run to deepen relationships and increase sales amongst the existing customer base.

Offer

How well the product/service meets its target markets specific need or desire.

Copy

How compelling the campaign messaging is so that it grabs prospects' attention, interests them and drives them to act.

A marketing channel is a specific route by which the company engages with its prospects. There are four principal channels:

1 **ONLINE**
Customers engage via websites, paid advertising and social media channels.

2 **DIRECT**
Customers engage directly with company salespeople (through showrooms, stores, exhibitions and offices, or field-based salespeople).

3 **INDIRECT**
Customers engage with a third party who sells the company's products/services. These include dealers, wholesalers, and aggregating websites.

4 **REFERRAL**
Customers engage with the company via existing customers through referrals and recommendations.

Companies that rely on a single marketing channel are vulnerable if it fails. Most companies have a range of channels and try to avoid excessive reliance on any one of them.

Prospects into customers

> **"Until you reach a million, it is ALL about sales"**
>
> Verne Harnish

I worked for a consultancy practice and was tasked with building sales relationships with large companies in the retail sector. The Managing Partner measured my progress using a straightforward tool. On his office wall was a simple funnel diagram like this one.

The critical steps in the sales process were laid out, and there was one golden rule. Every target had to move one step down the funnel each month, or I had to explain why.

Sales is the process of converting potential customers' interest into sales orders.

The way that interest is expressed depends on the channel they engage. For example, walking into a showroom, inbound phone calls, emails and website contact forms are all indications of interest.

Once a potential customer has expressed interest, the role of sales is to convert the interest into a purchase. This can involve anything from a thirty-second exchange at a cigarette kiosk where the customer knows the exact brand and quantity they want, to replacing a fleet of airliners requiring sales discussion over many years.

The discipline of selling has had to evolve because of the ever-increasing range of products, methods of purchase, and most importantly, the customer's ability to access all the information they need to choose a product without leaving their chair.

Social media, online forums, and websites also enable customers to research choices and gather other customers' views[11] .

Making sales is less about persuasion and more about building relationships and helping customers. Old school practices still exist, but they are rapidly heading for extinction.

Each customer will have their own unique criteria and method of making buying decisions.

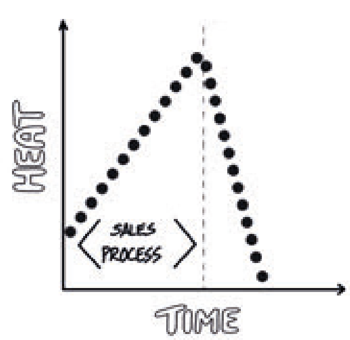
Good salespeople guide customers through a sales process that gives them the best opportunity to position their products/services.

Four things must be present for a customer to buy a product/service from a particular company.

1. Belief in the product/service, the salesperson, and the company. Customers will buy from people and companies they like and trust.
2. An opportunity to explain their needs, hopes and fears.
3. An understanding of how the company's products/services will benefit them and solve their challenges.
4. The opportunity to buy.

If the sales process is successful the customer will be excited and ready to buy. Asking for the sale at this point is critical[12] to avoid the impact of the law of diminishing intent.

The law of diminishing intent is that customers experience a sharp drop in their interest levels when given too long to decide. Doubt creeps in and other things demand their attention.



11. The potential customer can have as much, if not more, market knowledge than the salesperson.
12. Yet research showed that 70% of salespeople do not ask the customer if they want to buy the product/service.

Money on the Table

The famous McDonalds lines, “do you want fries with that?” or “would you like to go large?” add millions of pounds to their revenue.

A good sales process explores all options with the customer so that money does not get left on the table. Customers need to be aware of the range of options (and their pros and cons) and be offered additional products/services.

Measuring Sales Performance

The primary measure of a salesperson’s success is the rate at which they convert potential sales into actual sales. This is their conversion rate. It is most often expressed as a percentage (if a salesperson sits ten appointments and three of them become customers, her conversion rate is 3 in 10 or 30%).

The measurement of conversion rate provides insight into the performance of salespeople and helps them explore and refine their approach to selling.

Handover

Once a sale has been confirmed, many companies have a handover process. This involves all sale details being accurately communicated to the team preparing and delivering the product/service.

This is a common tension point in companies with delivery teams and sales teams blaming each other for not communicating customer requirements clearly or failing to deliver what the customer was expecting.

Delivering the Product/Service

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This is a common tension point in companies with delivery teams and sales teams blaming each other for not communicating customer requirements clearly or failing to deliver what the customer was expecting.

One of my clients had a customer who regularly purchased a custom product. The customer used to buy about four or five of the same products every month.

The product was packed and shipped as a kit, and the customer completed the final assembly.

There had been a couple of grumbles from the customer. Sometimes when they opened the box, the parts had moved about, and although the product wasn't damaged, it was difficult to empty the box and make sure they had all the components.

He could have bought the product from alternative suppliers, and my client didn't want to lose him.

The problem was solved by designing specific packaging at a minimal extra cost. As a result, when the customer opened the box, the components looked like a new set of Meccano, all laid out as they should be.

That change transformed that customer's experience and ensured their loyalty.

The delivery of the product/service to a customer can be as simple as placing it in a bag and wishing them a good afternoon or as complex as a project, spanning many years, with regular customer updates and interactions.

The delivery of a product/service occurs within a process (often referred to as the order-to-invoice process). This process consists of a series of action steps that should ensure:

- ***The customer gets the product/service they want.***
- ***The product/service is delivered in an acceptable timescale.***
- ***The quality of the product/service is what the customer was expecting.***
- ***The customer is kept aware of what is happening[13] .***
- ***Help and information are available when the customer needs them.***

The only opinion that matters when it comes to delivery is the customers. This influences whether the customer comes back or refers the company to others.

Customer expectations are set long before they decide to buy. They come from branding, advertising, the look and feel of the product, what other customers say, and what the salesperson told them.

When I shop at Lidl, I expect there to be long queues, that not everything I want will be in stock, and that I won't get that as warm as I get when shopping in Waitrose. My EXPECTATION of Lidl is not to feel like a god amongst men as I peruse the aisles. It is that my shopping is much cheaper.

Above everything, customers want a CONSISTENT experience. An experience consistent with what they expected and consistent every time they buy.

Fulfilling a customer order requires action from many different parts of a company. The difference between consistency and inconsistency is attention to detail.

Even if customers don't consciously notice the little things, they still 'notice' them. Therefore, particular focus should be given to customer touchpoints. These are the 'moments of truth' in the process, the steps that the customer sees or is involved in[14] .

13. If a customer has to chase or ask for updates, it is a reflection of a poor delivery process.
14. If everyone in the company did their job as if a customer was following them and watching their every move, it would always go smoothly.

The inevitable visit of Mr cock-up

One of my clients owns a restaurant. I remember a particular occasion when a customer had claimed that a meal had made one of their party ill.

The owner thoroughly investigated the cooking and preparation of the food and found no evidence to suggest that there had been a problem. Irrespective of that, I asked my client, "how have you responded to the customer?"

The owner had immediately invited the customer and their guests back for a complimentary meal. His awareness of the idea of turning a complaining customer into an advocate worked.

The customer went from being very unhappy to a regular visitor to the restaurant. WIN!

How you handle complaints matters[15]. It's a three-step approach with the goal of turning a complaining customer into a raving fan.

1. Fix it for the customer - then do something astounding for them[16].
2. Figure out what happened - the post-mortem occurs once the customer is happy.
3. Fix the process - to prevent a recurrence.

Complaints are gifts. They provide insight into how improvements can be made to the company.

But unfortunately, a company cannot buy this insight; only earn it by cocking up occasionally.

When is a customer not a customer?

One of my clients sold point-of-sale products to retail stores and product manufacturers. They set up a website with an online store and began to win sales through this channel, although the sales were low value and typically, the customers only purchased once.

A simple process was implemented to overcome this relationship gap.

The company began sending a letter to the customer after their orders had been fulfilled. The letter included a discount voucher for their next purchase and a copy of the product catalogue. In addition, they made a phone call to the customer to make sure they were satisfied with the product they received, find out more about what the customer did and introduce other elements of the product range to them.

This had the effect of building a relationship with the customer and getting them to purchase other products.

15. Research suggests that people tell, on average, eight other people about a problem they had with a company.
16. I refer to this as 'fixing the problem plus One'. One of my favourite examples is the restaurant story in this chapter.

A customer who buys from a company once is not a customer. They are a transaction. They become a customer when they buy several times and begin to build a relationship with the company.

I've seen it suggested that it costs, on average, seven times more to attract and win a new customer than it does to sell the same value to an existing one[17]. Once a company has won an order, the goal is to keep the customer buying.

At this point, it is necessary to capture information about them to grow this relationship[18].

Tesco is arguably one of the most successful companies at understanding complex customer spending patterns. Their super successful Clubcard lets them gather detailed information on their customers' spending, what they buy, and how often they shop.

Although launched as a scheme to reward the loyalty of their customers, the real juice in the scheme is the information and insights they have gleaned about customer behaviour.

With the right data collection, it is possible to better understand a customer's buying behaviour, including what they spend on what and when.

Over a more extended period, a company can build a profile of customers to anticipate their spending patterns and behaviour.

This means they can deepen the relationship by ensuring availability and advising the customer on new products or changes.

One of my clients identified major spending customers and held annual reviews with them. At these reviews, they talked the customers through their spending patterns and shared a report about the customers purchasing over the last year. This included recommendations for saving money and information about industry developments. The customers loved these reviews and began to view the company as a trusted advisor instead of just another supplier.

Ultimately, the goal is not just to have a satisfied customer, but one who willingly advocates the company, says nice things and provides referrals.

Referrals happen when a happy customer tells other potential customers about the product (in favourable terms). Therefore, the extent to which customers are prepared to recommend the company is the principal indicator of how good its products and service are.

Referrals can happen naturally or can be encouraged or rewarded. Thus, it is a delicate balance deciding when and if to actively request referrals and how the design of a referral scheme should operate[19]T.

Well-designed referral schemes benefit all three parties, the company, the referred and the referee, even if that benefit is a simple thank you.

Understanding which of the company's customers actively refer is essential to avoid upsetting high value referring customers. Their value to a company is way above what they might spend.

17. This is a dangerous and almost certainly inaccurate average, but the principle is sound.
18. It is becoming increasingly difficult to get customers to part with contact details for this very reason.
19. Some customers like to be rewarded for referring customers, while others may not be allowed, or want, to accept such rewards.

I visited a friend who lived in the Alps for a few years. An English couple runs a brilliant restaurant on one of the local slopes. Every Sunday, they do a traditional English roast, and with views over to Mont Blanc, it is about the most perfect place on the planet.

My friend takes all his visitors there, and over the years, I have recommended it to countless people.

He returned his main course on my last visit because it was too dry. The waitress bought a different course, and then one of the owners came over to speak to him. What I assumed was an apology turned into an argument about the meal not being dry. It was very unseemly and a bit embarrassing. He continued to be frosty towards us for the remainder of our visit.

I will not go there again and wouldn't recommend it anymore. How much future business did they will lose over whether that piece of duck was dry or not?

The goal is always to maximise the value of the customer over the lifetime of the relationship.

The ability to create recurring or ongoing revenue from customers varies from market to market. Still, any company should search for related products and services that can be offered to customers.

This creates a revenue tail that enhances the customer's lifetime value and keeps the relationship in place.

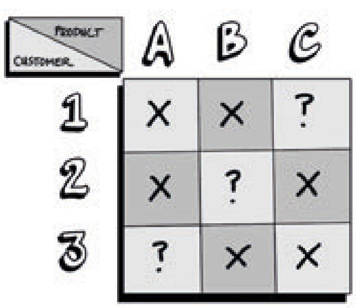
I have worked with several clients in the business of building swimming pools. But unfortunately, a swimming pool is the sort of high-value purchase customers only make once or twice in a lifetime.

One way pool builders overcome this 'lumpy revenue' profile is to offer service packages that keep the pool clean and ready for customers to swim in.

The customer can pay this charge annually, quarterly, or monthly. It gives the pool company a chance to smooth its revenue, and equally importantly, maintain a relationship with their customer.

This relationship keeps them in the loop for major plant replacement, refurbishment, and upgrade projects, as well as referrals.

Customers associate companies with the products they buy from them, but they may be unaware of the full range of what the company sells.



Understanding what each customer is and isn't buying from a company enables them to identify opportunities to upsell and cross-sell other products/services from their range.

A simple customer/product matrix allows companies to search for patterns and identify further revenue potential from their existing customers.

Keep in Touch

Competitors are always trying to steal customers.

Maintaining and nurturing customer relationships is essential whether the customer has a current transaction in progress or not.

Research into why customers switch suppliers claim that 68% change for nothing more than perceived indifference. In other words, they didn't think that the company was bothered whether they stayed or left.

Keeping in touch can be anything from a quarterly[20] email newsletter to a dedicated account management team, depending on the value of the customer to the company and the pace of change in what the company offers customers.

A two-way flow of information with customers provides market insights and an opportunity to sell additional products/services that could be of value to the customer.

Churn

One of my clients sells a service to other businesses based on a three-year contract.

The salesforce was increasingly struggling to sign new customers, and there was a lot of focus on improving their performance.

Early in the coaching programme, I asked about the renewal rate of customers reaching the end of the contract. The owners guessed it was around 90%, but I asked them to produce actual data.

The following week the scores were in, and it shocked the owners to realise that the actual rate of renewal was less than 70%.

This insight drove them to gradually transform their business. 'Lack of use' was seen as a critical indicator of a potential non-renewal, so proactive customer contacts were introduced when usage dropped and focus was put on improving customer service.

Acquiring new customers is expensive and hard work. The last thing a company needs is a leaky bucket that requires constant topping up with new customers.

It is not always easy to work out when a customer has stopped being a customer. Not every product or service has an 'off button', a trigger that notifies the company that a customer has left the building.

Systems are needed to identify good customers who are inactive and have stopped (or are likely to stop) buying.

20. This appears to be the minimum acceptable timeframe. If in doubt, the best thing a company can do is ask its customers.

When customers called in to cancel their contract with the mobile phone company, they were sent to the retentions team. This team was trained to try and persuade the customer to stay with us. They had a matrix of offers that they could offer to try and keep the customer, based on the customer's lifetime value and the history of their relationship with us.

Companies should try to re-engage customers who stop buying. At least they can find out why the customer decided to leave, and it may be possible to tempt them back.

Either way, the customer's expectation was not met, so they didn't buy again, and unless asked, they may never reveal the answers. This intelligence can be used to refine products, pricing, or delivery processes.

Ugly customers

Of course, there are some customers that a company would happily see appearing in the churn figures. The ones who drain customer services and account managers' time and energy, pay when it suits them, and put ridiculous demands on the company's delivery capabilities.

They are unprofitable, a strain on resources and a waste of energy. So, passing them on to may be the best strategy.

7 The Economic Engine

The economic engine describes how the company creates profit and cash flows through the business.

The historical weapon of choice used to measure the financial performance of companies are the accounts, submitted each year. They consist of the PROFIT AND LOSS ACCOUNT, BALANCE SHEET, and CASH FLOW STATEMENT (depending on the company's size).

These records are not very useful for helping drive a company forward.

The problem with these records is that:

They are designed primarily for consistency and the benefit of the taxman.

They involve judgement and estimates that can bear little resemblance to actual performance

They are snapshots at a specific point in time.

They are 'after the event', with the timescales of HMRC seemingly more critical than the commercial feedback they give the business.

In this section, we will initially look at the structure of the core financial reports because it is valuable to know.

But there are four super helpful numbers that I try to understand in every company I work with.

1. **Acquisition Cost** - how much it costs you to acquire a new customer. Whilst that may not seem relevant to all companies right now, I promise you that it's going to become very important at some point soon.
2. **Customer Lifetime Value** - how much gross profit is a customer worth to you throughout their entire engagement with your company.
3. **Execution Margin** - the profit actually made on a sale compared to how much the company expected to make.
4. **Leverage Ratio** – The amount of fixed cost per pound of sale value.

When we understand these four numbers, in conjunction with the financial records, we have everything needed to figure out what is going on.

Finally, we'll focus on cash and talk about how companies drive and use money.

The Traditional scorecard

I remember watching an American Football game on T.V. during my first business trip to the States. It was all very colourful and occasionally exciting, but ultimately dull. My *interest level deteriorated because I couldn't keep up with what was going on. Statistics flashed over the screen, and I couldn't navigate my way through them to even figure out who was winning. I switched off.*

For business, the scoreboard is the accounts, so anyone interested in the company's performance should have the ability to understand the reports, at least at a basic level.

There are three principle financial reports that companies use to report their performance to their investors, shareholders, and the Inland Revenue:

PROFIT AND LOSS ACCOUNT
The report shows how much net profit the company made and how that was achieved.

BALANCE SHEET
The balance sheet provides a view of what the company owns and what it owes.

CASH FLOW STATEMENT
This shows the movements and sources of cash coming in and out of the company.

The report most managers head for first is the profit and loss account, whereas investors make a beeline for the balance sheet.

The documents need to be used together for a complete performance picture to emerge.

The numbers are more valuable when there is something to compare them to, such as the company's targets or the performance over the same period last year.

Profit and Loss - Did we win the game?

The profit and loss account is the scorecard for the game. It shows whether the company made a profit in the period. The key numbers are:

SALES - Sales is the value of sales the company made. This might be actual takings, orders received, or confirmed commitments, depending on the company's accounting policy.

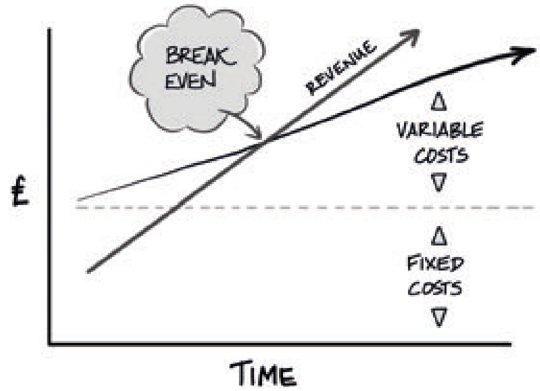
COST OF SALES - The cost of sales (also sometimes called variable costs) is the company's costs to buy/manufacture the products they sell. This typically includes any stock, raw materials, or components. Some companies may also include other costs such as productive labour, allocations of overheads, sales commissions, and some marketing costs.

GROSS PROFIT - Gross profit is the difference between the value of sales and the cost of sales. It is usually expressed as a value and as a percentage. The gross profit percentage will vary wildly depending on what the company sells.

OPERATING COSTS - Operating costs (sometimes referred to as fixed costs because the company incurs them whether it sells anything or not) are the general expenses the company incurs. This includes the costs of people (salaries, benefits, training), rent and rates, utilities (light, heat, and power), repair and maintenance, advertising and marketing costs.

NET PROFIT - Net profit is the value left when the fixed costs are taken away from Gross profit.

BREAK-EVEN – Break-even is when a company generates enough sales to cover all of its costs. It looks like this:



A business operating below its break-even point is in a loss-making position and vice versa.

Massaging the numbers

Accountants make several assumptions or estimates in most profit and loss accounts.

The three most important ones are:

BAD DEBT PROVISION - This is an allowance in the operating costs for customers not paying for the product/service they received.

DEPRECIATION - This is an allowance made in operating costs to account for the reduction in the value of fixed assets (machinery, vehicles, plant and equipment) over time). It spreads the loss of value over time rather than just taking a hit at the end of the asset's life.

MATCHING - To make the gross profit figure mean something, the cost of sales must be matched to the actual sales in the period. This is known as the matching principle, and it ensures that the Gross margin is as accurate as it can be.

The Balance Sheet - what shape are we in?

The balance sheet was named because it does precisely that, balances.

There is a simple equation to understand a balance sheet:

CAPITAL + LIABILITIES = ASSETS

CAPITAL - This can be made up of money the owner or investors have put into the business in return for owning a share of the company.

LIABILITIES - These are the amounts the company owes to other organisations and are split into:

- ***Long Term Liabilities, which include mortgages and bank loans.***
- ***Short Term Liabilities include money owed to suppliers, money paid by customers for services not yet delivered, and short-term financing tools, such as overdrafts.***

ASSETS - This is the actual value of what the company owns. These are split into two/three categories.

Current Assets are assets that are, or can quickly be turned into, cash. This includes debtors (money owed by customers), prepayments (payments made to suppliers in advance of them providing services), stock, and of course cash itself.

Fixed Assets are assets such as property, plant and machinery, and investments the company owns.

Intangible assets include brands, designs, and goodwill.

The balance sheet enables investors and other interested people to understand how the company's value is made up and funded. The balance sheet is also used to determine how much a company is worth in conjunction with trading performance.

The balance bit of the balance sheet now makes perfect sense. A company can only have assets equal in value to the money initially put into it.

A company's value is not based solely on the value of its assets. For example, a company may only have a few fixed and current assets. Still, it may have an enviable customer base, access to a particular market, a great piece of intellectual property, or a strong relationship with some important suppliers. This may make it particularly attractive to a company looking to expand its own reach.

If company A has an asset value of £50m, and company B purchases it for £75m, the £25m difference is known as GOODWILL.

Cash-in, Cash-out

The cash flow statement shows cash movements in and out of the company and the sources.

It indicates whether the company has sufficient funds to meet its commitments and sustain itself without external funding. It is very similar to a standard bank statement, except it categorises cash flows in and out under three types of activity:

OPERATING ACTIVITY
Inflows will be from sales or interest receivable. Outflows will be supplier payments, payroll and interest.

INVESTMENT ACTIVITY
Inflows will include cash from selling assets and loans from customers. Conversely, outflows will be purchases of assets or loans to suppliers.

FINANCING ACTIVITY
Inflows will include cash from investors, shareholders, or lenders. Outflows will be dividends and repayments.

So there you have it; the formal financial records in simple terms. Now let us turn our attention to four commercial numbers that really matter.

Two of them are from the realm of sales and marketing (Acquisition cost and Customer Lifetime value), and two relate to margins (Execution Margin and Leverage ratio).

Acquisition Cost

When mobile phone technology became available, handsets were given to customers for free when they signed up for a contract[21]*.*

This proved so popular with customers that it went on for many years.

Roughly, if you signed up for a £40 per month 12-month contract, the operator gets £480 of guaranteed revenue. This all seems sweet until you consider that they give you a handset with a value of at least £250. Also, if you took your contract out through a dealer, they get paid a commission.

There were also network connection costs paid to other operators.

After everything was paid out, we were left with an average gross profit of about £70, per contract per year.

These days, businesses face intense competition for customers because the internet disrupts historical geographic and market niches.

Companies must invest money in marketing/sales to attract and connect potential customers to the company[22]. This is the **ACQUISITION COST**.

The amount that a company is prepared to spend to acquire new customers will be a proportion of the level of profit a customer produces over the lifetime of their involvement with the company (see customer lifetime value) as follows:

Acquisition Cost < Customer Lifetime Value = Good Business

Acquisition Cost > Customer Lifetime Value = Crap Business

Without measuring acquisition cost, it is hard to establish how marketing spending returns on investment[23]. But, on the other hand, if the acquisition cost is well understood, marketing can be seen as an investment with a rate of return[24] .

Customer Lifetime Value

Most companies have a good grip on the value, transaction volume and product breakdown of their sales number. This is useful, but the critical number to understand is the customer lifetime value.

This is calculated as follows:

(Average Order Value X Number of Transactions) / number of customers

21. To drive the uptake of devices and also to attract customers to particular networks.
22. Even if companies don't think they need to do this at the moment, it is only a matter of time until they'll need to.
23. In the absence of an understanding of acquisition costs, Marketing budgets often get viewed as operating cost.
24. The simple maths here is that if I offered you a deal where for every £1 you gave me, I gave you £3 back, how many £1s would you give me?

It can be measured at a company, individual customer, or customer class level.

Customer Lifetime value is a critical number for two reasons:

> ***1. It enables acquisition costs to be understood so that a suitable marketing model can be developed for the company (see above).***
>
> ***2. It is an indicator of the effectiveness of a company in acquiring, retaining, and developing customer relationships (especially when tracked over time).***

Execution Margin

The financial goal is to make a profit margin that reflects the level of investment/effort put into the company.

Profit margins are tracked at two levels.

Gross profit is the difference between the value of sales and the cost of sales.

Net profit is the value left after fixed costs are taken away from Gross profit.

A profit margin is made when there is a positive gap between the value of sales and the business's costs. Margin can be expressed as a number, e.g., we made £50,000 profit, or as a % of sales, e.g., 25% profit.

Execution margin is the difference between the planned gross and net margin[25] and the achieved margins.

Gross margin can be improved by either charging more for products or lowering production/purchasing costs.

Charge more (or at least don't discount)

A customer's willingness to purchase a product depends on the value they perceive the product/service has relative to the alternatives.

Research indicates that 80% of buying decisions are emotionally led and 20% logical. It is rarely a simple mathematical choice.

Prices of products should be continually reviewed and tested to ensure maximum margins are achieved without significant loss of market share.

Sometimes price increases can improve gross margin, even if some customers stop buying.

The table below shows the percentage of sales that could be lost without any bottom-line impact, based on different price increase/margin scenarios.

PRICE INCREASE \ MARGIN	20%	40%	50%	60%
2%	9%	5%	4%	3%
10%	33%	20%	17%	14%
14%	41%	26%	22%	19%
20%	50%	33%	29%	25%

For example, if a company increased a product selling price by 10%, it could afford to lose between 14 and 33% of its customer base, depending on the product gross margin.

Some products are more price-sensitive to customers than others[26]. This is because the cost of these products can influence a customer's 'feel' for the companies pricing.

25. The margin that the company set out to make in its budgets, forecasts and operating plan.
26. Particularly ones that are bought regularly, are essential but unexciting purchases or have little differentiation between choices.

Lower production or buying costs

The cheaper it is for a company to buy the things it needs to make products or buy stock, the better its margin.

Getting cheaper stock, materials, or components often involves committing to larger or fixed volumes. This becomes a trade-off between tying up cash and additional storage costs vs improved margin.

Prices can be improved through negotiation and by working with suppliers to engineer value to enable both parties to make margins. This extends beyond price discussions but takes a bigger view of the relationship.

Even when pricing is set well and the cost of sales are fully optimised, there are still ways that margins can 'leak'.

Keeping the profit margin on target requires that complex variables work correctly. Margin leakage can happen through:

- **Discounting and pricing errors** – Discretionary and unplanned price reductions.
- **Quotation and pricing errors** - Getting the price or estimates in proposals wrong.
- **Errors and rework** - Time and materials to correct faulty products or sending the wrong product to the customer.
- **Waste materials** - Raw materials wasted in production.
- **Billing errors** - Failing to bill a customer for all of their received products.
- **Theft/fraud** - Fraud by employees, suppliers and customers can occur.
- **Damages and write-offs** - Damage to stored products and the write-off of 'out of date' or obsolete stock.
- **Returns** - Failing to account for products and materials returned from the customer and suppliers.
- **Collection of discounts** – Failing to collect discounts due from suppliers.

Leverage Ratios

One day, I discussed margins with one of my clients who has a Quantity Surveying practice. His business is a classic 'time for money' trade. He submits a proposal based on how many days of effort the job will take, adds his margin, and bingo. We were looking at recently completed assignments, and they came in on budget. If he quoted ten days, they were taking ten days. So, the job should have been delivered with a margin bang on target. Yet when we looked at the profit and loss account, the margin was a fraction of what was budgeted. There was leakage.

When we looked at the numbers, one of the challenges was that the team was only utilised for 70% of their working week. The other 30% was made up of some rework and non-productive time. So virtually the entire margin in the jobs was being lost.

The owner set a target utilisation rate for the team that enabled the business to make the required margin and introduced utilisation rate to his business dashboard.

Achieving net profit margins is not only about keeping gross margins under control.

It also requires that other business costs are minimised (without undermining the service and quality that the company strives to achieve).

All companies drive greater efficiency in manufacturing products or delivery of services to grow margin and remain competitive. This may mean investing in technologies, better design and scheduling of production, or looking at alternative means of production and delivery, such as sub-contracting and outsourcing.

Keeping costs under constant scrutiny is essential for any company[27]. However, these challenges require creative thinking to deliver as trade-offs have to be considered in any changes.

The highest operating cost for many businesses is payroll and the associated costs of people. So it is little wonder that the staff budget and getting maximum utilisation out of people is critical.

High costs can also result from over-servicing customers, 'blinging[28]' assets, the cost associated with industry processes and currency fluctuations.

Understanding the impact of reductions is vital. If costs are removed from customer-facing or impacting teams, the results can be seen and measured quite clearly. However, back-office reductions seem to have little or no immediate effect. The impact takes longer to become visible or can be an opportunity cost that never becomes fully visible.

Fixed cost reductions that are not resulting from leveraged solutions are never impact-free.

The best way of tracking leverage is by using a ratio. The exact ratio used will be different for each company but will relate sales or gross profit to fixed costs. Some solid examples include:

- **Profit per employee.**
- **Fixed cost per unit.**
- **Sales to fixed cost ratio.**

When tracked over time, this ratio gives essential information about whether the company's leverage is improving or not.

Show Me the Money

"Turnover is vanity; profit is sanity; cash is reality."

Every businessman that ever lived

27. I was annually set a 15% cost reduction challenge in my operational role.
28. Spending more than necessary on business consumables and equipment

One of my swimming pool building clients did a lot of installations as part of larger construction projects. As a result, the pool build timetable was subject to delays and rescheduling based on progress with the broader project.

Payments were made by the main contractor to a pre-determined submission timetable.

The business had high fixed costs to meet, so even with a volume of ongoing projects, there were often periods where there was little revenue coming in. The owner often had to fund the business through these periods with personal money and would get very upset and frustrated, claiming that the team was not properly managing the projects and the payment submissions.

As a result, he refused to entertain the idea of other short-term funding, such as an overdraft facility.

It looked more like a cost of operating in the sector they worked in. It was unlikely industry payment processes would change, and there was a limit to the improvements that could be made internally. A better approach was for them to understand and manage the company within this constraint.

The ultimate goal of a company is to create a surplus of cash. It is the oxygen of business, and the lack of it is why most failed companies stop trading.

It is essential to distinguish between cash and profit as they are fundamentally different.

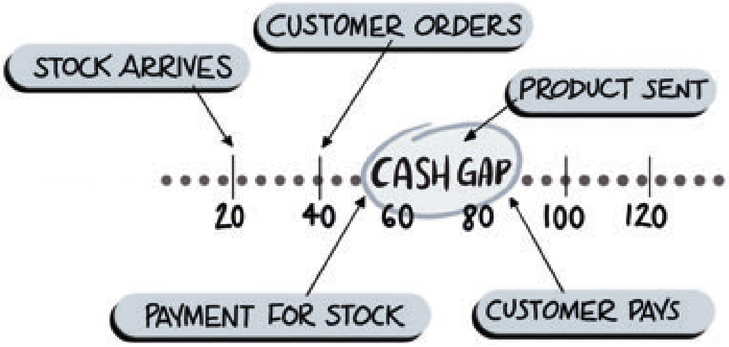
If you started a company and made sales of £100 with costs of £60 in June, when I go to check your bank account, I would expect to find £40, right? WRONG.

This transaction would appear on the profit and loss report as follows:

	£
SALES	100
COST OF SALES	(40)
GROSS PROFIT	60
COSTS	(20)
	40

Whilst the sale and the cost of sale appear in the June profit and loss report, the actual movement of cash relating to these transactions can be quite different.

Let's look at the actual cash movements.



1. ***Stock or raw materials are purchased.***
2. ***The customer orders.***
3. ***Payment is made for stock or raw materials.***
4. ***Product is sent to the customer.***
5. ***The customer pays.***

This timing difference is known as the cash gap. The significance and impact of the cash gap vary from industry to industry and company to company.

Ideally, every company would prefer to receive payment up-front. Thus, they would always have money in the bank (provided they made enough sales). However, some companies can sell their inventory and bank the cash long before paying for the products/services in extreme cases. This creates a positive cash gap.

Commercial reality does not work like that for the bulk of companies.

I started to coach a printing company. During our first session, the owners informed me of how dire the financial situation was. They needed to invest in new business marketing, but they were financially hedge hopping (flying far too close to the ground), and the overdraft was maxed out.

If some more work didn't come in within a few weeks, they were going to hit the ground. So, I asked how much money the business was owed. They didn't know. So, I gave them 24 hours to produce a schedule of completed work that had not been invoiced and invoices sent to customers that had not been paid.

The following day I revisited them, and the schedule showed £10k worth of work waiting to be invoiced for, and over £50k outstanding with customers, some of it overdue by months. So I made them stand up and walk out to the front of the building, where I looked up at the wall and said, "Well, where is the sign?"

They looked at me bemused, so I pointed to the signage. "I can't see the word bank in the description of your company. Go and get that money." After that, the business was back on financial track, and we began discussions about marketing strategies.

Understanding the cash gap is vital because a company has to have sufficient cash to fund the gap and its growth and sustainability goals, either through building reserves or borrowing.

Both of these options carry an opportunity cost. Reserves could be used to fund further growth, and borrowing incurs interest, which eats into profit margins.

Minding the cash gap

Good cash flow control is a function of speeding up cash inflows and slowing down outflows.

A company will do what it can, subject to what the customer wants and suppliers are prepared to work with, to optimise its cash gap through a combination of:

1. Speeding up the money coming in by having fast invoicing and strong credit management.
2. Slowing down the money going out by negotiating extended credit terms with suppliers or tighter management of stock levels.

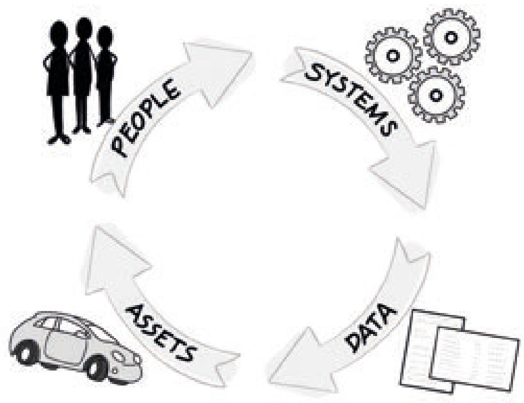
There are trade-offs with managing the cash gap. For example, it is possible to alienate customers by being too heavy-handed with credit management. Similarly, suppliers can become unwilling to supply if payment delays are excessive, creating a cash gap problem.

What to do with the surplus?

The surplus of cash created by company activities can be used in several ways:

- ***Expansion of the business through new products and entering new markets.***
- ***Acquisition of other companies that complement its activities.***
- ***Payback debt that the company owes.***
- ***Returning to shareholders in the form of share dividends.***
- ***Investing in improving the company and creating a more leveraged business.***

8 Structure



In this simple model of companies, the structure is how the company's assets are organised and operated.

A company's assets include the people, equipment and resources it uses to deliver value. These are organised into processes and functions, managed through communication and data.

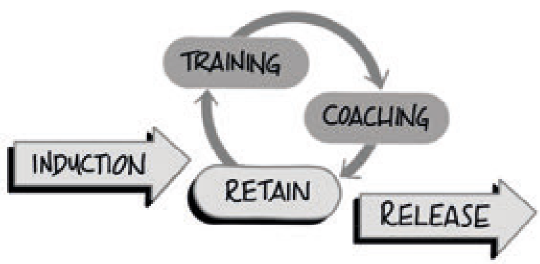
The structure exists to:

1. Consistently deliver the required standard of customer experience and product quality.
2. Uphold the reputation of the company and its position in the marketplace.
3. Deliver the desired level of profitability to the company.
4. Grant minimum energy, effort and cost.

Company structures should be kept under constant review to identify opportunities for advancement and efficiency.

This is the principle of leverage.

People



People are the most significant expense for many companies.

They bring the human touch, creativity, problem-solving, skills and knowledge that animates the company and brings it to life.

They are also expensive, inconsistent, prone to error and vulnerable.

Managing people is about harnessing the best aspects of human behaviour and minimising the worst.

In the interests of efficiency, people are organised into teams based around functional specialisms (sales, manufacturing, finance) or business units (geographical, market or product divisions).

All organisation structures have inherent tensions resulting from conflicting functional goals and priorities[29] . An effective organisational design efficiently delivers the company's goals while minimising functional tensions' adverse impact.

Cross-functional communication, data flow, and coordination are vital considerations in designing an organisation structure.

29. One of the commonest being the inevitable tension between sales and operations.

The role of specific individuals is typically set out in job descriptions and through target and objective setting.

Desired behaviours to be demonstrated by employees are set out in policies or enshrined in company values.

Once explicitly defined, the required performance of individuals is managed through induction (when the employee is new), training, coaching, and performance review.

People are supported in their roles by assets, including computers, machinery, tools and equipment.

Systems

Activities are organised into systems that attempt to deliver consistency for customers and internal efficiency protecting and ensuring margins. However, the extent to which behaviours and methods are prescribed depends on how important consistency and efficiency vs flexibility and innovation are in driving quality, service and margin.

Repeating activities are organised into processes that deliver consistency for customers and internal efficiency. These are laid out in procedures, checklists, or system-based rules that enforce or prevent certain behaviours.

I.T. systems drive further consistency, accuracy, and efficiency and produce valuable business data for decision-making.

Data

Data is both an input into the structure and an output. It is needed so that decision-makers can establish whether:

1. The company is doing what it is supposed to be doing.
2. The company is achieving its desired outcomes or not.

Data is essential for planning, measurement, decision making and the regulation of the company and its performance.

This data can be both quantitative and qualitative, and a good structure enables it to be captured and shared across the company.

Key data elements include:

MARKET DATA
information about the size of the market, customer behaviours and preferences.

OPERATIONAL DATA
metrics about marketing and sales, manufacturing operations, service levels, quality and customer satisfaction.

FINANCIAL DATA
Information about profitability, margins, sales, valuation and cash flow.

Assets

All businesses deploy assets to deliver value, and there are broadly two classes.

Fixed Assets are assets that are expected to be used in the long term in the company. They include buildings, vehicles, plant, machinery and I.T. equipment. The focus in managing **fixed assets** is to maximise the utilisation of the asset whilst minimising the cost of owning and operating it.

Current assets are directly used in the delivery of products to customers. They include raw materials and finished goods. Managing **current assets** balances the cost of purchasing them and holding them with availability.

Leverage

One of my clients is in the automation industry. Specifically, they work with machine vision technology that allows complex robotic automation.

Paul, the owner, showed me an application they had been developing.

It was in a factory that processed Brussel sprouts ready for retailers. Around thirty employees were employed in doing two simple operations on each sprout that passes through the factory.

Firstly, they check the sprout for its quality and remove any rotten or imperfect ones.

Secondly, they trim the stalk off and cut a cross in the sprout with a knife.

No biggy, you might think. But when I tried to get my head around how you could automate this process, I began to struggle. Brussel sprouts are not uniform in size or shape and, when dropped onto a conveyor, will be pointing and sitting in different positions.

I understood how a robot arm could operate in an environment where every sprout presented to it was identical and delivered in a predictable way. But how could the technology know whether a sprout was the right quality and figure out which way to orient it for cutting?

That's where the machine vision systems come in, and once it was explained to me, I realised that technology would change everything.

Each sprout passes under a camera that captures an image of the sprout. The system is trained to look for a sequence of colours. The shape and colour of the leaves give a hint as to where the stem is located. The robot arm knows whether to dispose of the sprout or, if it passes quality control, exactly how to pick it up and orient it to pass it through a water blade, which cuts it.

If it can't match the sprout to an image, it simply sends it round a loop where the sprout is agitated before passing it under the imaging system a second time.

Competition demands continual focus on the improvement and efficiency of the structure.

Leverage is the continual search to achieve more with less.

This can be as simple as working with an individual to improve their performance, redesigning a process or restructuring functions. Of course, these day-to-day improvements cumulate to enhance overall effectiveness, but there are three strategic leverage points to be considered.

1. SYSTEMISATION
The relatively low cost of I.T. systems and the increasing ability of these systems to 'think' and make decisions for themselves through the application of A.I. will increasingly reduce the need for people[30].

2. OUTSOURCING
Many companies already have external service providers to deliver non-core activities (Finance, H.R. etc.) when it is more efficient to do so. The introduction of I.T. platforms that can operate as intermediaries between companies and service providers from all over the world[31] and the relatively low cost of offshoring will continue to drive structural change.

3. AUTOMATION
The increasing sophistication and reducing cost of robotic automation will become a driver of productivity for many companies, eliminating manual jobs, professions and trades that traditionally relied on people.

The challenge for company leaders is to balance the need to remain cost and quality competitive in their markets with the desire to continue to provide high-quality employment to a committed and motivated team.

> **"When we demand that our workers engage in a race to the bottom with any country willing to work faster and more robotically, we take something away from the people we work with"**
>
> *Seth Godin*

The drive to create leverage results in a high-risk trade-off. Systemisation, automation, and the relentless drive for efficiency eventually conflict with our desire to connect with others and express ourselves through our activities.

Customers want a good service and a personal touch to their interactions with a company.

Demand for consistency and efficiency can dumb down roles until all skill and 'art' are lost[32].

We deny employees job pride and satisfaction and then wonder why they disengage from their work and company.

30. Even those in historically 'safe' professions such as accountancy and law.
31. The production of this book was done in no small part through individuals I have never met.
32. The art is the employee's ability to express something of themselves through their work and their connections with colleagues and customers. Its loss is closely followed by loss of pride and satisfaction in the role.

WORKING WITH DAVE

If you and your leadership team find yourselves not moving forward at the speed you could; if you are caught up in 'busy-ness' or mired in complexity and uncertainty; perhaps a conversation with Dave is just what you need.

The presenting symptoms could be

- *A feeling of stuckness or that progress is not as fast as it could be*
- *Overwhelm and a sense of hamster wheeling*
- *A workforce that doesn't appear to be inspired or motivated to push forward*
- *Complexity makes it difficult to see the commercial wood for the trees and execute on meaningful priorities*
- *A lack of cross-functional and big picture thinking*
- *An inability to lead, inspire and create motivation in their teams*
- *A lack of confidence and resilience, so difficult conversations and actions get avoided*

Through his content, talks, facilitated workshops, training programs, or coaching, Dave helps individuals and companies transform in profound ways.

His simple and powerful approach helps people create shifts that don't just energise companies, but that transform people in ways that they will find useful throughout their entire careers and lives.

His straightforward, direct, and engaging style gets people thinking differently about their company, work, and themselves. It's grounded in a depth and breadth of commercial and leadership experiences that bring the ideas to life.

- *A career leading various organisations from small professional teams, complex cross-functional programs and operations.*
- *Twenty years in Corporate Audit putting all aspects of a company under detailed commercial scrutiny.*
- *Advanced coaching and transformational capabilities developed through his career and finely honed by heavy investment in his skill set.*
- *Thirteen years working with Small and Medium-sized businesses ranging from £2-120m turnover across a wide range of markets and sectors.*

You can find out more and book a conversation with Dave at www.sixthsensebusiness.com or simply email Dave (dave@sixthsensebusiness.com).

"Dave's Great! Always full of ideas, optimism and humour, but at the same time a level-headed businessman. I really enjoy our meetings, always get something out of them, and really appreciate the wide blend of business skills he brings to a discussion (Marketing, Financial, Operation, H.R. etc.). I've not come across a business coach with such a breadth and depth of knowledge before. I'd definitely recommend his services"

Anthony Buxton – Managing Director (Premier BA)

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