BusinessPlus+ Newsletter

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Merry Christmas and Best Wishes for 2021!

Know the Financial Impact of Decisions Before You Implement Them

This is a strategy that many businesses are starting to implement, and it is generally known as "predictive accounting". The process starts with examining the physical number of units to be produced and the calculation of the direct costs that will be involved in that process.

The calculation of stock holdings can be made based on manufacturing/purchase estimates and the unit sales based on estimates from salespeople. These estimates should be checked to determine the level of investment in stock to determine whether that level of stock is going to be required.

From the sales department estimate of sales a calculation can be made as to what the debtors' balance might be based on targeted debtors' days outstanding.

Consideration could be given as to how debtors' days outstanding might be able to be reduced through quicker dispatch of tax invoices to customers, highlighting the due date for payment on the tax invoice, ensuring that any other information that the customer has requested is sent to the customer with the tax invoice so that there is no excuse for payment delay, prompt preparation and dispatch of the debtors' statement and the ongoing follow-up of customers whose payments are outside the negotiated payment terms for that customer.

The cash effect of these purchase decisions and receipts from customers for both cash sales and credit customers can then be shown in the Cashflow Forecast for the business.

If you are contemplating a major expenditure item such as business expansion, or a major research and development project (where, whilst you might be entitled to a Research and Development Incentive Rebate you will not receive the benefit of this until the next financial year), scaling up your business so that you can increase your turnover - this normally involves additional investment in stock and debtors and perhaps in additional premises.

All of these costs need to be examined and factored into your financial projections.

What is the result? Do you have the financial capability of funding these extra activities?

What is the shortfall? Will you be able to borrow the shortfall from a bank? Will you have enough security available for the bank to secure the extra loan? Are you and your colleagues happy to sign personal guarantees and to commit to monthly principal and interest repayments?

Are you interested in exploring the opportunities for your business to be able to raise capital direct from the public?

Companies can raise capital as follows:

- Under Section 708 of the Corporations Act, a private company can raise up to $2 million from a maximum of 20 investors in a 12-month period.
- Crowd Sourced Funding Equity Raising was legalised in Australia about 3 years ago by amendments to the Corporations Act to enable a private company to be able to raise up to $5 million in a 12-month period.

Young companies (normally under 3 years of age, but in some cases up to 6 years of age) that have been involved in the development of a new product, process, service, marketing or management methodology can raise capital from investors who can obtain a tax offset on their personal taxation debt and possibly avoid paying capital gains tax.

To raise capital from the public, companies need to produce a Business Plan, Market Position Report, Marketing Plan, Budgets and Cashflow Forecast and Business Valuation.

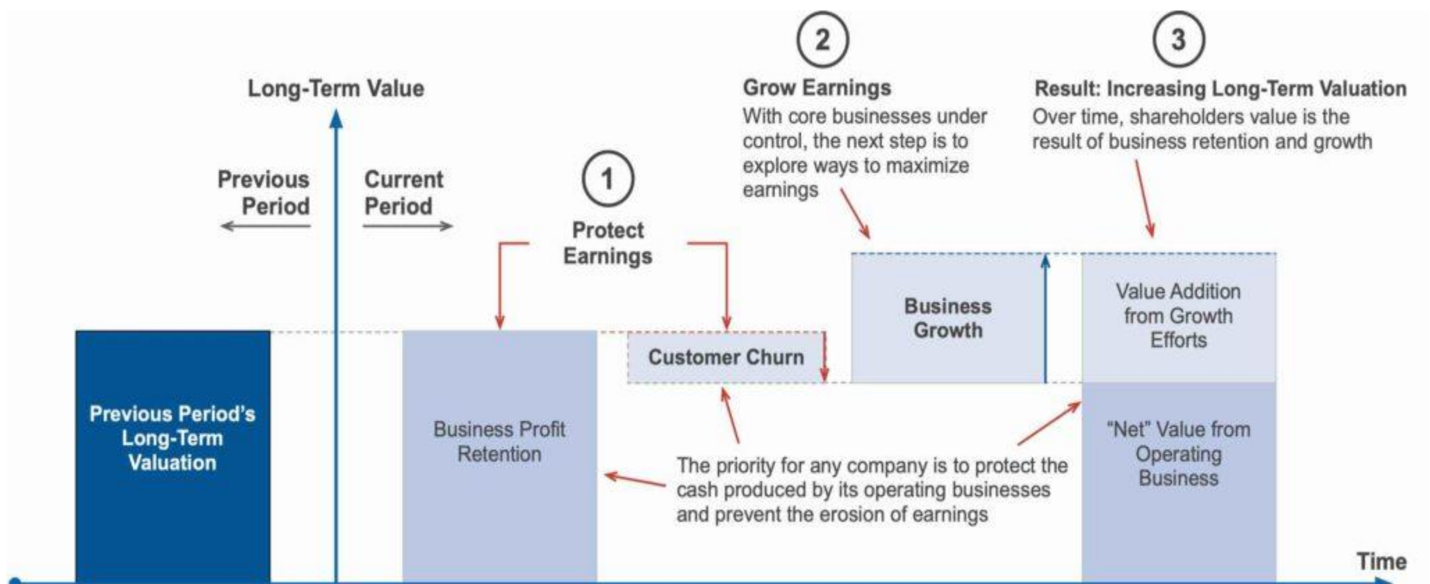
This has been a brief overview of knowing the impact of financial decisions before you implement them. If you would like to discuss this type of analysis for your business, please contact us at CBSW.

The Fundamentals of 'Business Strategy' - Part 2

The fundamental concepts of business strategy haven't changed much over the last few decades. What has been taught in business schools since the early 1980s are still the pillars that support most of today's strategy frameworks.

But rather than having changed, our knowledge of strategy has "evolved" significantly now that we've had the opportunity to experience longer periods of competition and to observe the rise and fall, sometimes miserably, of companies and businesses once regarded as the most innovative like Toys R Us, Blockbuster, Kodak and Border Books.

The starting premise for a successful business: there are only two things that management must do well - protect earnings from the operating business and maximise earning's growth over the foreseeable future. That combination of defend-and-grow is what builds an organisation's value over time, as shown in the diagram below.



***Maximising shareholders' value takes a combination of initiatives to both defend and grow core earnings. That combination is what grows a company's valuation over time* and is at the core of *modern business strategy*.**

If during a given period management does nothing else but ***to protect the company's earnings*** from erosion and grow those earnings at the level or even higher than other high-performing companies (not only industry competitors), most people (especially shareholders) would agree that they have done a great job and that the business's strategy has been successful.

Secondly, let us remind you that ***the profit formula only has three components: Price, Demand** and **Costs***, and that consequently, a good strategy is one that either helps us sustain premium prices or superior levels of demand, or one that help us lower unit costs.

A business decision that doesn't help you achieve either of those two goals should not be considered part of your business's strategy.

Respect Trumps Harmony - Five Leadership Lessons from The World's Toughest Workplace

By *Rachael Robertson* ***

Leadership is an intrinsic part of everyone's workplace, no matter the role you're in. Australian - Rachael Robertson, led an expedition in Antarctica for a year and since her return has become an author, keynote speaker and leadership expert. Rachael's leadership and teamwork skills were put to the test during her time in Antarctica and in this article, she shares crucial leadership lessons developed from her time there. These lessons are relevant to all of us and may be applicable in your business team.

The Antarctic winter is harsh—temperatures hover around –35 degrees Celsius, there are constant blizzards, months of darkness, and you can't get in or out. Work becomes tedious and your sense of purpose is sapped by the knowledge that nothing will change until the re-supply ship arrives, a distant nine months away.

It sounds extreme. But the reality is every workplace has an Antarctic winter. Every business has a period where the work slows down, and work is just work. There are no big, challenging projects on the horizon and capital expenditure slows to a trickle. In these times, more than ever, leaders must find ways to inspire their people and retain the best staff, ready for the inevitable up-swing.

In Antarctica I used five tools to keep my team, and myself, inspired and motivated through the long Antarctic winter.

No Triangles—the practice of only having direct conversations, built respect within my team and resulted in very high performance. We had a simple rule: 'I don't speak to you about him/her and you don't speak to me about him/her.' No Triangles. Go directly to the source.

It's a powerful tool that reduces conflict and clarifies accountability. The practice of No Triangles also ensures your time as a leader is spent dealing with issues that matter, issues that will have the most impact on the organisation. Not burning up your energy handling personal disputes.

It also shuts down 'answer shopping'—people who keep asking the same question, going over people's heads, or around people, until they get the answer they want.

Manage your Bacon Wars—a major dispute over bacon threatened to shut down our Antarctic station: should the bacon be soft or crispy?

Every workplace has their "Bacon Wars". They are seemingly small, irrelevant issues that grate on people, but build up over time until they become distractions and affect productivity. It may be dirty coffee cups; people who are consistently late for meetings; people playing on phones while someone is presenting…they appear to be small offences but, they are usually a symptom of a deeper issue.

Leaders must identify and probe their "Bacon Wars". Find out what's underneath and resolve it.

For us, it turned out the "Bacon War" was a manifestation of something deep and important: respect between two teams.

Find a Reason to Celebrate—recognise milestones and important moments. If you don't have one readily apparent, then create one. Find a reason. In Antarctica we celebrated big events but also the smaller successes such as a month without a power blackout, significant scientific data collection or a period of uninterrupted internet access with a fully functioning server.

Usually it was just a notice on the whiteboard in the dining hall, but it was important to find the time to stop and celebrate. ***Why - because these moments create momentum. They give a sense of progress, of moving forward and getting closer to our outcomes.***

Peer Support Is Gold—leadership can be a lonely road. As leaders we must retain a strong boundary between ourselves and our staff.

I had no one I could talk to about issues on our station, but I did have a peer at one of the other Australian stations. I could phone this Station Leader and explain what was going on with confidence that he would fully understand. He'd call me and I'd have the same empathy.

A colleague who understands the challenges of your role; someone you can relate to and can discuss options with, is something to foster, nurture and treasure.

Respect Trumps Harmony—my expedition team was the most diverse team I've ever worked with. I didn't recruit them - I was handed them. We were from vastly different backgrounds, a mix of professional skills including scientists, engineers, IT, trades, pilots and weather specialists. The only generalist role was mine: Station Leader.

With such a mix of people, it was impractical to think we'd all get along with each other all the time. The interpersonal pressure was intense, and privacy was scarce. It would be unreasonable to expect total harmony, so I didn't. ***Instead, we aimed for respect - simple, professional courtesy and respect.***

I have grave concerns for any team that, explicitly or implicitly, strives just for harmony at the expense of productivity and respect. It's dangerous for two main reasons. Firstly, dysfunctional behaviour continues, it just goes underground so the illusion of harmony remains. Secondly, it stifles innovation. People are often too afraid to put up their hand and offer a different view or opinion because they don't want to rock the harmony boat.

Instead of harmony, teams should aim for respect because 'respect trumps harmony', every time.

***** Rachael Robertson has written two books on leadership – "Leading on the Edge" and "Respect Trumps Harmony".***

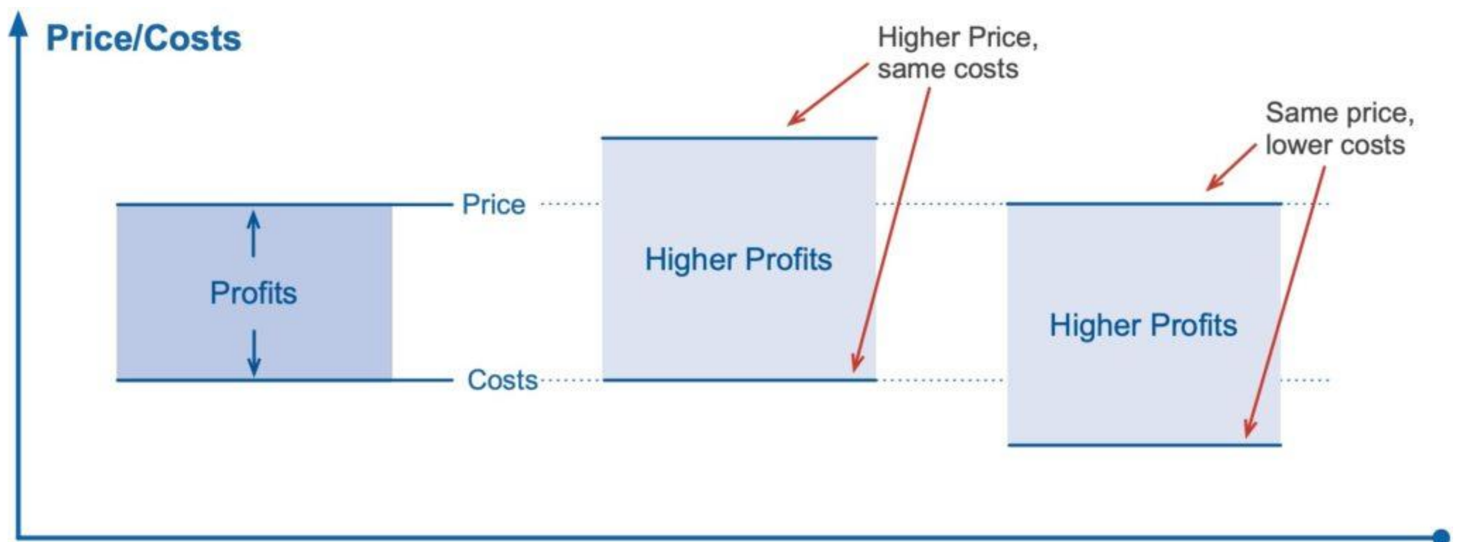
Profit versus Profitability

The Profit Equation

The profit equation only has three variables: price, volume and costs.

Price x Volume = Revenues; and
Revenues - Costs = Profits (Losses)

That means that to increase profits all you need to do is to increase sales (either by increasing prices or driving more demand), reduce costs (or get higher productivity relative to your current fixed costs), or achieve some combination of the two. The diagram below clearly illustrates these inter-relationships.



How Price and Costs Affect Profitability

That seems like a very simplistic definition, but the underlying implications of these relationships go well beyond that formula since profits, as we will see, connect to everything a company does.

For example, revenues, through sales, connect a company's products and services with its customers, its distribution channels and its sales force, while costs on the other hand interface a company's offering with its operations and supply chain.

The way you create wealth for a company is by maintaining a healthy balance between revenues and costs over time.

In general, the wealth-creation cycle happens in three steps. First, you sell products and services that create ***Value*** for customers. Second, you retain a piece of that value in the form of ***Profits***, and third, you transform those profits into ***Cash***, which is the ultimate goal of ***Strategy***.

With this cycle in mind, you could define profitability **then as a measure of the *wealth* that a company gets to keep for itself from the creation of value for customers.** That wealth, however, must later be converted into cash, which is the final prize. It is hard cash not profits, that you can use to pay bills, grow the company and pay earnings to shareholders, **therefore cash, not profit, is the ultimate goal of strategy**.

The role of strategy, therefore, is in providing a plan that helps a company retain as much value as possible in the form of "cash", provided that such a plan is sustainable over the long term through sustainable (and growing) profitability.

The profitability that a company can achieve in any given market will be restricted or "constrained" in some way by the influence of different factors that work inside and outside the organisation, including:

Business Choices about Product Design: Decisions about the features and benefits that your products and services offer, and how well those align with the identified needs of your target customers. Since you are only able to capture a fraction of the value created, the more value your products create for customers the more you can target to keep for yourself.

Structural Factors in Our Core Markets: The relative power of the players in the markets where your products and services are sold defines to some extent how the value that you create must be *shared* with those other players. If you are a powerful incumbent, you get to keep a bigger share of the value you create; if not, better positioned players will command a bigger piece of the action.

Structural Factors in Adjacent Markets: Similarly, the nature of adjacent markets or industries where your competitors, customers, vendors, substitute products and complementary offers operate influences their power to claim a bigger share of your product's core market. Vendors that are powerful in their industry for example, can make you pay more for their products, getting a bigger bite of your profits.

Official Regulations: Regulators, in the form of government, lawmakers and others, can limit the profitability of an industry through laws, taxation and incentives. Mature industries will naturally have the most established regulation

frameworks, but in emerging one's regulation will be weak or even lacking, presenting an opportunity for savvy executives to be part of how that regulation is shaped.

Non-Market Factors and Trends: Factors outside the market itself such as prevailing industry standards (or lack thereof), state of technological development, labour and unions, predominant working style and cultural norms may influence how value, and in turn profit, is created. Similarly, observable trends and industry evolution might also affect the space of potential profits in the foreseeable future.

Each of these factors can affect your ability to claim a bigger share of the value you create for your customers, and your strategy is in a way your response to your understanding of those factors, which means you should really understand them very well before you can come up with a winning strategy.

It is your job as a business leader to understand how these factors are having an influence on your company's performance. You may have the best strategy and still get poor results if your market sucks, in the same way that you could get great results with a poor strategy in a thriving market.

But at any given time, you should be able to say what is driving unusual performance of the market. Is it because of a market trend; Competitors behaving more or less aggressively; Regulators tightening or loosening things up; OR is it because the market is growing too fast or too slow?

Common Misconceptions about Profits and Profitability

Before we move on, it is important that we clarify a few misconceptions about critical concepts when it comes to strategy and profits.

Market Share and Sales DO NOT Guarantee Profits: Increasing sales and market share doesn't automatically mean higher profits. Any company could increase sales significantly by pricing products and services below cost (losing money of course).

Sales and market share only provide an indication of revenues, but revenues alone don't make profits, as they don't consider the costs associated with those sales.

Being Bigger Doesn't Guarantee Profits: Another misconception is that being bigger than everybody else, because of the economies of scale you create, is how you beat competitors. In reality, scale alone cannot ensure higher profits. ***Economies of scale do exist and are very important, but they dissipate fairly quickly in many industries, and once that happens, they no longer provide a competitive edge.***

Beating Competitors Doesn't Guarantee Profits: Kicking rivals out of business will not ensure higher profits unless you beat ALL your competitors out of the market.

Being unique and achieving superior returns should be your goal, but beating rivals is not a strategy.
Innovation Doesn't Guarantee Profits: Innovation is expensive, difficult and can't ensure your products will be overnight hits. In fact, most innovation attempts fail by big numbers.

Explaining Differentiation Strategy

The aim of any business organisation is to find a market position for its products and services that is both profitable and defendable in its market of choice, and such a position can only be achieved through differentiated products or lower relative costs, that is, by either doing different things from competitors, or doing the same things in different ways.

How to Differentiate Your Products and Services

A differentiation strategy should translate into higher prices, higher demand or both. Lower costs, on the other hand, should translate into lower prices (which should lead to higher demand), higher margins or both.

The main goal of a company pursuing a differentiation strategy is to influence the perception of value about its brands in the minds of target consumers. Being *perceived* as being more valuable than other alternatives by those customers is what drives the company's ability to raise prices or sell more, and without that perception a differentiation strategy will not succeed.

In general, there are four levers that executives can use to influence such perception:

Differentiated Products: Offering products and services that are both unique and valuable to target customers. These products may be continually improved and augmented along dimensions that matter to customers, to reduce business erosion.

Differentiated Promotion: This means experimenting with different promotional tools and messaging campaigns or testing proven campaigns with new customer segments. Strong brands can play a big role in differentiating a company's offerings especially in crowded markets.

Differentiated Sales and Distribution Channels: Distribution channels and sale efforts bring prospective buyers and customers together. At the end, the real demand reachable by a product is not the number of people who would like to buy it, but how many of them the product can reach.

Pricing Differentiation: In most markets, price can be used to influence demand and adjust customers' expectations of value. Companies must intimately know their markets and use pricing strategically to target both consumers and non-consumers.

You may use these four levers to influence the perception of value in the minds of your target consumers, however, what really gives you an edge is not whether or not your products actually deliver more value, but the *perception* that they do.

As a business leader, you must continually monitor this perception and take proper action when necessary.

The teams out in the field must produce reliable information about these perceptions, to enable executives to make educated decisions. They must keep their ears on the ground, tracking changes and trends in the marketplace, and use their knowledge and expertise to produce information that can be acted upon.

There are many tools available, perception maps for example, that can help measure the positioning of a given brand in the minds of target consumers, relative to other product servings in the same market.

The goal of a differentiation strategy is not to compete with rivals and take them out of business, but to find a position that is both profitable and defendable, and in that position, you may co-exist with other companies within the same market.

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