

# Growing Smarter

## Three Strategies for Managing Your Growth Successfully

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### Part I

There's a good reason why 80% of the companies in the landscape industry do under 1 million dollars in annual sales. Early success in growing a business does not necessarily lead to success later on. The tactics that produced your early successes are not the same ones you need to grow profitably. That's because increased size – in terms of sales volume – changes the game of running a business. Smaller companies run very successfully using an operator style. Operators control everything, know where everything is, prefer seat of the pants decisions making, and value people with the same "just do it" attitude that the operator applies to getting the work done. Larger companies are unable to run profitably using an operator style; they instead must use a manager style to produce profits.

Managers do not control, they instead systematize and plan to produce profits. The fundamental management rule is – look before you leap. The operator's maxim on the other hand is; leap, then we'll look as we are going. As a result operators can produce great results and great disasters. So why don't operators change and why don't we see many more multi-million dollar landscape companies? The truth is, most operators prefer to be operators. They enjoy shooting from the hip and have a hard time planning. This does not mean that they do not grow, they do. And when they do their style gets them into trouble. In the best of cases, the trouble they get into forces the operator to retreat and regroup, often by reducing sales and staff. And in the worst of cases, it can strand the opera-

tor in a "no-man's land" scenario where they can struggle for years with mediocre profits, before going out of business.

Operators – by definition – grow "out of control." "Out of control" means growth without the checks and balances of a plan. Lacking a plan, no owner or manager can effectively address the challenges of increased complexity and risk. Complexity and risk can turn uncontrolled growth into the worst-case scenario. Let's take complexity first. As sales increase, so do the number of interactions among people and customers. While sales will always increase in an arithmetic fashion, complexity grows geometrically. In simple terms this means there are a lot more problems to handle everyday for the operator. The second challenge is increased risk. The consequences and costs of a bad decision increase with size. Simply put, smaller companies make smaller mistakes, and can recover more rapidly than larger companies. Risk compounds complexity. Not only are there more potential

problem and mistakes, there is an increasing probability that one of these will be a very costly mistake.

A simple example illustrates the nature of increased complexity that comes with rapid growth. Table 1 shows the growth of a \$400,000 company over five years. The first row shows annual sales, the second row the growth rate. The third row shows annual sales increases. Rows four and five show average customer sales size and sales by FTE (refer to the definition later on in this article). From these numbers it is easy to calculate the increased number of people and customers. Row eight, uses as a baseline a single interaction per day between the operator and his people, and the operator and his customers. As you can see by the end of five years, while sales have tripled, complexity has increased by almost fourteen times! This increase in complexity is the direct cause of profit declines. No operator can end-run this phenomenon. They can only plan for it.

TABLE 1

	1997	1998	1999	2000	2001	2002
Sales	\$ 400,000	\$ 520,000	\$ 676,000	\$ 878,800	\$ 1,142,440	\$ 1,485,172
Growth Rate		30%	30%	30%	30%	30%
Annual Sales Increase		\$ 120,000	\$ 156,000	\$ 202,800	\$ 263,640	\$ 342,732
Average Sale	\$5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000
Sales per FTE	\$60,000	\$ 60,000	\$ 60,000	\$ 60,000	\$ 60,000	\$ 60,000
Number of customers	80.0	104.0	135.2	175.8	228.5	297.0
Number of people	6.7	8.7	11.3	14.6	19.0	24.8
Number of annual interactions	360	360	360	360	360	360
Complexity	192,000	324,480	548,371	926,747	1,566,203	2,646,883

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To control growth and maintain profits, operators need a simple planning system. In Part I and II of this article, we offer some simple planning approaches and philosophies, and provide examples to help any operator put on the manager's hat. There are three basic strategies in the planning system. These strategies are titled **organization**, **market position** and **capital**. In Part I, we discuss **organization** and **market position**. In Part II, we outline approaches for managing finances and **capital**. To begin, let's define the problems associated with the lack of strategy before outlining the planning approach.

**ORGANIZATION:** You not only need people to grow, you need organized people. The first focus of planning must be – people. Smaller companies succeed *because* the owner makes all the important decisions and every job is everyone's job. These same factors cause larger companies to grow "out of control". It is not possible to run a larger business where the operator is a bottleneck and jobs overlap randomly. Decision-making is too slow and inflexible, and when all jobs are everybody's job, they end up being nobody's. Growth must be controlled within a staffing plan and an organization chart.

**The organization chart:** Planned specialization is part of controlled growth. There are three primary functions in a growing business. These are sales, operations and administration. Adopting a manager style means that the operator must give up two of these functional hats to focus on one. This doesn't mean that the operator is un-involved in the other two areas. It simply means that the operator must choose one job and hire people for the other two jobs. The best job for the owner in my opinion is the sales job. The companies that grow most profitably in the industry - in my experience - are those where there are two key people in the beginning. These people are alter egos, who split sales and production and delegate full responsibility to the other to run that function. And if they are smart they have at least one full time staff person in the office to handle the paperwork *before* they reach one million dollars in annual sales.

**The staffing plan.** The growth of staff cannot outrun the growth of sales. Planning for the right staffing levels requires the use of two key ratios – the *realize rate* and the *sales per FTE rate*. The realize rate is calculated as follows: Annual sales divided by the number of

paid production hours. The sales per FTE rate calculation is: Annual sales divided by the number of full time equivalent people on payroll. The rule is grow staffing only as fast as you grow sales. If these two ratios are declining in a given year so are your profits. To establish a staffing plan use the two ratios as illustrated below. Refer to Table 1 – Years 2001 - 2002.

### STAFFING PLAN

	2001	2002
Sales	\$ 1,142,440	\$ 1,485,172
Growth rate	30%	30%
Annual sales increase		\$ 342,732
Production Hours	40,000	52,002
FTE's	18.5	24.05
Realize rate	\$ 28.56	\$ 28.56
Sales per FTE	\$ 61,754	\$ 61,754

In 2001, a profitable year, the company paid 40,000 production hours to foremen and crews, and employed a total 18.5 Full time equivalent people during the year - including the owner/manager. This calculates into a realize rate of \$28.56 per hour and a sales per FTE rate of \$61,754 per person. Knowing these numbers the manager can establish a staffing plan that uses these rates as a planning check and balance to plan for the right staffing level. As you can see from the example, in 2002, a 30% growth rate translates into \$342,732 more sales. The ratios tell the manager that the maximum allowable FTE staffing level is 24 people and 52,000 production hours. The manager can now control growth by planning for, and monitoring these target rates. Exceeding these rates reduces profits.

**MARKET POSITION:** You not only need more customers to grow, you need more of the right customers. The second focus of the plan must be – customers. Smaller companies succeed *because* of long-term relationships, pricing, and word of mouth advertising. These same factors cause larger companies to grow "out of control." Over-reliance on long-term relationships and pricing structures reduces flexibility and profits. It is not possible to grow a business where older customers and outdated pricing schemes eat up profits that need to be funneled into new equipment and staffing. Growth can only be accelerated by updating pricing and developing niches that

have the effect of clearing out customers who no longer fit with your route or production structure.

**Pricing/Productivity:** Prices must keep pace with rising costs and productivity performance. Planning for price increases must be a part of every plan. This does not mean that you will make price increases everywhere and at the same rate, because productivity gains must be worked into the equation. Planning for price changes requires the use – again – of the *realize rate*. The rule is: pricing or productivity increases must pay for the increases in your cost structure. To determine your pricing plan use the realize rate as illustrated in the example. Again refer to Table One – year 2001.

### REALIZE RATE

2001	Actual Client A	Target Rate
Invoicing Hours	40,000	1550
Realize Rate	\$ 25.81	\$ 28.56
Difference	\$ 2.75	
Price Increase	10.7%	
Decrease Hours	149	
Increase rate	9.6%	

As you can see in 2001, a review of the client list shows that client A contributed \$40,000 in invoiced sales at the cost of 1550 production hours. This produced a \$25.81 per hour realize rate, far below the target rate of \$28.56. There are at three ways to increase the rate. The first is to install a price increase of 10.7% (the \$2.75 difference divided by the \$25.81 realize rate). The second is to achieve a productivity gain of 9.6% (reduction of hours by 149). The third is some combination of price increase and productivity increase to adjust the rate. Price planning includes an account-by-account review to determine target-pricing levels for both existing and new business. The manager can now control growth by determining contract pricing and productivity goals.

**Niche Development:** Customers must appreciate your price / product proposition or they should be cleared from your base. Planning for growth means targeting markets, not revenue additions. Controlled growth requires niche development. A niche is a market segment where your price / product offering is appreciated by a particular class or customer type. Adding or keeping unappreciative customers

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reduces profits in the short and long term. In the short term you may reduce prices to get the work and crowd profitable work out of your schedule. In the long term, the problems generated by this customer class increase hours, and eats up profits and patience. Planning requires the use of the 80/20/30 matrix. Refer to Table 2 below.

Table 2 shows customer class in descending order of sales volume in the first column. Class A customers are large customers. The range column describes the percentage of the customer list in that class – the top and mid-top 20%. The Sales volume column describes the total volume of sales for that class as a percent of the company's total revenues. The Action column describes the rule for developing the niche or clearing it out. To conduct the analysis, arrange your customers or accounts in descending order of annual sales volume. Segment the top 20% of the list into Class A, the second 20% into Class B and so on. The first rule is to increase prices or productivity by the "Action" percentage in the third column. The second rule is to increase the focus on pricing

**TABLE 2**

Customer Class	Range	Sales Volume	Action
A	Top 20%	60%	2%
B	Mid top20%	20%	5%
C	Mid bottom30%	10%	10%
D	Bottom30%	10%	15%

ing actions as you "go down" in class on the list. For example, for the bottom 30% of the list, all the 15% action may be in the form of a price increase, whereas all the 2% action at the top of the list may come in the form of a productivity gain (hours reduction). The manager can now control growth and profits by target price and productivity increases.

Lastly, the manager can control growth by focusing efforts in developing a true selling function. If you recall the organization chart strategy from earlier in the article, you remember that the operator is now freed up to wear one hat and pursue a focused sales effort full time. This

approach is far better than relying on word of mouth advertising to grow your niche and your profits. All these strategies are designed to create a planned and controlled growth effort.

In Part II, we will focus on the third strategy – capital. In Part II we describe several key planning ratios that address budget building and the determination of a realistic equipment spending plan. For the operator, executing simple planning checks and balances can mean the difference between out of control growth and its attendant profit problems or success both financially and personally.

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