BUSINESS FORUM

Building by the Numbers

by Les Cunningham

Too many remodelers can't improve their firm's bottom line because they have no idea what it is. Here's how to find out where you stand.

If your firm is doing under $1 million in annual sales volume, you should be paying yourself, as the owner, 20% of the gross in total compensation. The first step toward achieving that goal is to develop mission statements for yourself, your family, and your business. All three statements must be going in the same direction at the same time, all of the time.

Next, you have to figure out where you are and how far you have to go. The only way to do that is to compile all of your business data in a logical order that enables you to see your starting point. Over many years of conducting financial audits for remodeling companies, I've developed a form that allows you to track your company's crucial financial numbers (see chart).

The figures shown are real numbers from real companies. In my business workshops, the owners of noncompeting companies gather together and fill out this chart for each of their companies. A collection of all of the charts is given back to the participants to analyze prior to the meeting. The results are discussed over the course of a three-day workshop in the hosting company owner's hometown. The participants take apart the host's business in a positive peer-review process, then put it back together better than it was before. One outcome is a two-year business plan for the host company to implement. This plan is tracked via follow-up reports to the group every six months.

The companies involved in these meetings are broken into two segments: companies with sales ranging from $100,000 to $1 million, and companies with sales ranging from $1 million to $7 million.

The chart shown here presents averaged data for the companies with which I consult. They are not what *your* numbers should be; rather, they establish the key line items that I believe you must be able to track if you are to determine reliably your own expenses and profits.

Emerging Trends

The numbers on the chart were compiled during the recent recession — 1989 to 1991. After reviewing the averages — as well as the raw data from which they are derived — I have noticed several trends.

Trends under $1 million.

- A company that grows too rapidly loses money. Usually, this is because the owner isn't up to speed with the management skills required to be profitable at this pace.
- During slow times, smaller companies become more frantic to get business and less selective in the jobs they accept. This often results in an additional loss of money.
- To keep jobs coming in, many companies cut out the cushion they usually include to protect against jobs that don't go exactly as they were bid. Inevitably, this comes back to haunt them.
- During tough times, companies tend to decrease their advertising and marketing budgets without knowing how this will affect their business, other than the notion that it will save money. While doing so helps control direct costs, cutting back in this area also makes you less of a presence in your market, and eventually costs your company more.
- Small companies tend to give too much to their employees (such as fully paid insurance) without first considering how these benefits will affect the finances of the owner and the company.
- Owners intermix their personal and professional lives too much. For instance, they often will borrow money against their home as collateral to keep the business afloat. As they lose more operating capital, they are at serious risk of losing their home and disrupting their family environment as well as their business.

Trends over $1 million.

- Company owners becomes focused so much on increasing volume that they fail to weigh the potential financial gain against the increased risk. As work volume goes up, so does overhead, and the return on investment decreases.
- When times get tough, these companies do a better job of management because they have more leeway to cut back.
- Larger companies win bids at higher prices than smaller companies, but 20% of their bid profits slip through their fingers.
- More and more owners of larger companies realize that they can't do it all by themselves, and they are taking a team approach to running the company.

Other trends. Here are some other points to keep in mind as you check the numbers on the chart.

- When the market begins to drop, the jobs get smaller, and the big commercial firms begin to muscle into the territory formerly held by the niche remodelers. At the same time, however, the number of small repair and replacement jobs increases, and the smaller companies are better able to pick up this business.
- In bad times, revenues for smaller companies may actually go up, because they start lowering their prices to win any job that comes along. Since not all jobs are profitable, however, these companies are misled into thinking that they are making money on jobs that are actually costing them money.
- Smaller companies have a harder time controlling their costs because they don't have the systems in place to do it. That's why costs for such items as building materials, payroll, and insurance begin to grow for

Common Income Comparison Form

	Category	Companies Under $1 Million 1991	Companies Over $1 Million 1991
1.	Commercial Work	9%	14%
2.	Residential Work	86%	76%
3.	Other	5%	10%
4.	Total Revenue	$603,000	$1,400,000
5.	Building Materials	26%	19%
6.	Payroll – Labor	18%	9%
7.	Payroll – Project Manager	1%	4%
8.	Payroll – Taxes	2%	1%
9.	Employee Benefits	1%	1%
10.	Subcontractor Cost	31%	29%
11.	Insurance	3%	1%
12.	Vehicle Expenses	1%	1%
13.	Design/Engineering Fees	<1%	<1%
14.	Permits	<1%	1%
15.	Sales Costs	<1%	2%
16.	Other	<1%	3%
17.	Total Direct Costs*	84%	69%
18.	Gross Profit*	24%	31%
19.	Advertising	1%	>1%
20.	Marketing	1%	>1%
21.	Bad Debts	1%	<1%
22.	Donations	<1%	<1%
23.	Entertainment	<1%	<1%
24.	Payroll – Design	<1%	1%
25.	Payroll – Supervisor	1%	1%
26.	Payroll – Taxes/WC	1%	<1%
27.	Employee Benefits	<1%	<1%
28.	Equipment Cost	<1%	<1%
29.	Interest/Bank Charges	<1%	<1%
30.	Tool Repair/Replace	<1%	<1%
31.	Employee Training	<1%	<1%
32.	Vehicle Expenses	<1%	<1%
33.	Total Variable Overhead*	6%	7%
34.	Payroll – Office	3%	4%
35.	Payroll – Owner	8%	4%
36.	Payroll – Taxes	1%	1%
37.	Employee Benefits	1%	1%
38.	Vehicle Expenses	1%	<1%
39.	Trade Associations	<1%	<1%
40.	Dues/Subscriptions	<1%	<1%
41.	Insurance – General	1%	<1%
42.	Taxes	<1%	<1%
43.	Legal Expenses	<1%	<1%
44.	Accounting Expense	1%	<1%
45.	Training – Owner	1%	1%
46.	Rent	<1%	1%
47.	Repairs/Maintenance	<1%	<1%
48.	Communications	1%	1%
49.	Utilities	>1%	>1%
50.	Total Fixed Overhead*	20%	14%
51.	Net Profit Before Taxes*	–8%	10%

* Totals are calculated as a percentage of total revenues. Due to rounding, totals may not agree with a sum of separate items.

The author asks his clients to fill out this chart every six months as a way of tracking revenues and the real costs of doing business. The numbers presented here are averaged from data submitted by more than 100 remodeling firms.

smaller firms as times turn tough.

- The 1991 "Net Profit Before Taxes" for small companies is not encouraging (see final line of chart). This is a direct result of some of the firms involved doubling their volume to keep jobs pumping through. Ultimately, these companies lost money because they didn't keep track of all their costs.

Where do you go from here? How do you avoid becoming one of those firms that grew in size but lost its shirt? The first step is to fill in the chart and take a look at your numbers. If your numbers are better than those shown here, then you're above average compared with the firms I've been working with. If you're below average and want to improve, you'll know where to start making some changes.

To grow as a manager and business owner, I recommend that you read the following books in the following order. When you're done, read the first one over and over until you can "walk the talk."

Seven Habits of Highly Effective People by Stephen R. Covey (800/553-8889). This book teaches you how to set up your life, your family, and your business.

The E' Myth by Michael Gerber (800/221-0266). This book clearly tells you what is required for you to have a better chance of making it in your business.

Guerrilla Marketing by Jay Conrad Levinson (800/748-6444). A good source for ideas on marketing your company in your local area.

The Unnatural Act of Management by Everett T. Suters (800/242-7737). This book illustrates how family businesses work, and provides some ideas about how to handle a business when the founder dies. ■

Les Cunningham spent 15 years running his own remodeling company. He now operates Business Networks, a consulting firm that conducts peer-review workshops with more than 100 remodeling companies nationwide.