Two Keys to a Company's Success

By Ralph Gotto

Many owners of small businesses and executives of larger companies (I'll call them "Leaders") find it difficult to grow their company; and once they have grown it, to maintain their competitive edge. The truth is, there are only two things you have to do well to gain or maintain the competitive edge.

Using these Two Keys will ensure the growth and competitive edge of your business. Many Leaders believe that companies more or less run themselves, i.e., as sales are brought in, all company spending appears to happen automatically in support of the sales.

In fact, one of the biggest mistakes that Leaders make is concentrating on sales growth. But sales growth will happen more rapidly and easily if you concentrate on these Two Keys.

What are these Two Keys to success that you have to concentrate on?

The Keys to Success are to: 1) become the #1 or #2 lowest-cost producer of products or services; and 2) become the #1 or #2 producer of high-quality products/services.

Are these Two Keys the only ones that matter? No, other things matter, too – people, equipment, and capital, just to name a few. But, being the lowest-cost and highest-quality producer are the most important for growing your business and gaining the competitive edge.

The Competitive Edge –
How to Gain It and Maintain It

Consider the following example: You have ten competitors in your particular product or service market niche. Two are at the top in low cost and high quality. Four are in the middle for quality and cost. Four are at the bottom for cost and quality.

. . . you can only gain or maintain market share by being # 1 or #2 in cost and quality.

Without this, the best marketing and sales programs will only have a short-term effect and no long-run sustenance.

Cost Structure – Typical

#1 and #2 have a 10 percent cost advantage over #3–#6, and a 20 percent cost advantage over #7–#10.

#1 & #2	Revenue	$100
	Cost	$ 50
	Gross Margin	$ 50
	Expenses	$ 35
	Net Profit	$ 15
	Net Profit %	15%

#3–#6	Revenue	$100
	Cost	$ 55
	Gross Margin	$ 45
	Expenses	$ 35
	Net Profit	$ 10
	Net Profit %	10%

#7–#10	Revenue	$100
	Cost	$ 60
	Gross Margin	$ 40
	Expenses	$ 35
	Net Profit	$ 5
	Net Profit %	5%

When #3–#6 try to take market share from #1 & #2.

Since #3–#6's quality isn't quite as good as #1 or 2, they can only take market share by cutting price. Most customers won't switch for less than a 10 percent price advantage.

If #3–#6 cut prices by 10 percent, the results are:

#3–#6	Revenue	$90
	Cost	$55
	Gross Margin	$35
	Expenses	$35
	Net Profit	$ 0
	Net Profit %	0%

#3–#6 cannot sustain this pricing very long, as it is a losing battle. If #1–#2 cut prices by five percent, it forces #3–#6 to cut prices by 15 percent, causing them to lose five percent on the bottom line – a going-out-of-business curve.

When #7–#10 try to take market share from #1 & #2

Since #7–#10's quality isn't quite as good as #3–#6, and way less than #1–#2, they can only take market share by cutting price significantly. For #7–#10, they must cut prices by 20 percent to take market share.

If #7–#10 cut prices by 20 percent, the results are:

#7–#10	Revenue	$80
	Cost	$60
	Gross Margin	$20
	Expenses	$35
	Net Profit	($15)
	Net Profit %	(19%)

This is a going-out-of-business curve. No company can sustain a 19 percent loss on products for more than a few months, and it takes a year or more to gain market share.

As these examples demonstrate, you can only gain or maintain market share by being # 1 or #2 in cost and quality. Without this, the best marketing and sales programs will only have a short-term effect and no long-run sustenance.

Bottom line,
being # 1 or # 2
in cost and quality
are the Two Keys
to a company's

Current Economic Downturn –
Why this may be the best time to concentrate on cost and quality.

With the current economic downturn, sales are slowing, with customers reluctant to spend, now and for some time to come; so when buying does return, you'll have to offer a quality product that provides a great Return on Investment (ROI).

How do you get costs down, you ask? By looking at your total cost chain, not just product cost. For example, you need to review the following:

Cost Chain Elements

Sales Price

- Are you pricing yourself as a leader in your industry?
- Remember, industry leaders can command a 10 percent advantage.

Manufacturing Costs

- Raw Material?
  What percent of total product cost?
- Labor Dollars?
  What percent of total product cost?
- Manufacturing Overhead?
  What percent of total product cost?
- Through-Put Time cost?
  How can we shorten it?
- Cycle Times costs?
  How can we speed them up?
- Quality Assurance costs?
  Can we lower with better manufacturing processes?
- Refurbishing costs?
  Can we lower with better manufacturing processes?
- Maintenance cost?
  Can we lower with better manufacturing processes?
- Delivery/Shipping cost?
  Is there a more efficient way?

Marketing Costs

- How many leads?
- What is the leads conversion percentage?

Advertising Costs

- Types of advertising?
- How many advertising pieces?
- What is the response rate?

Sales Costs

- What percent is salespeople's salary and commission?
- What is the productivity of salespeople?
- What is the sales closing percentage?
- What are the sales discounts?
- What are the quantity discounts?
- What are the sales returns?
- What rebates are we giving?
  What's it costing?

Research and Development

- What percent is Research?
- What percent is Development?
- What is the Time to Development?

General and Administrative Expense

- What percent of Revenue?

People

- Do we have self-starters?
- Have we continued to weed out the lowest performers?
- Have we done it each year?
- Most companies have 10 percent they can weed out with no adverse effect.

Assets Receivable

- What are your days of receivables?
- Are we collecting on time?
- Do we have too many delinquencies?
- How many dollars (what percent) are over 30 days old?
- None should be over 90 days old.

Inventory

- How many dollars are tied up in inventory?
- How many days of inventory do we carry?
- Every day of inventory is extra dollars of borrowing needed.
- How old is the inventory?
- Any inventory over one year is a write-off waiting to happen.

Accounts Payable

- What are your days of payables?
- Are you stretching your payables beyond 30 days?
- If not, you're burning additional cash.

This cost chain analysis will give you a good start toward becoming the lowest-cost producer, and will improve your product's quality, too.

We've been talking about a manufacturing company here, but the same process applies to a service business – you may not have the manufacturing or inventory costs, but the other elements apply.

Bottom line, being # 1 or # 2 in cost and quality are the Two Keys to a company's success.

Once you have accomplished cost reduction and improved quality, you're then positioned to capture market share and maintain it. **N**

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