How to stay in profit through 2007

In the second of a two-part feature, **Stuart Jackson** takes a closer look at how retailers can ensure a profitable 2007.

In December's feature we examined the generally flat retail outlook for 2007 and in this competitive environment for sales, it is critical to focus on the key performance generators of a retail shop.

In this issue let us remind ourselves which are the most financially rewarding elements of our business, for without a profitable foundation retailers will be unable to deliver their ethical goals.

The UK is fourth bottom of the EU economic growth table and for us retail is currently a poor performer, yet the Bank of England continues to support high interest rates to peg back inflation and house prices. To ignore this state of affairs risks the deterioration of shop profit to the point of critical failure or at least to where one's earnings are significantly reduced.

For most independents who receive accounts only annually, news of a crisis could first arrive when cash flow disappears. Better to act now.

That is a vaguely ominous picture to paint and generally I much prefer to focus on the positives, however, at the beginning of 2007 it is worth being brutally realistic about the facts if only to drive home the need to redouble our efforts. There is still no doubt that proactive retailers are succeeding.

The three key performance generators are: wages costs, Gross Profit percentage and sales revenue.

Wages

In an independent health food shop, wages can reach more than 20 per cent of annual shop turnover and a massive 60 per cent of overhead. It is singularly and by far the largest burden on business.

With retail sales growth in decline and individual wage rates on the up (via minimum wage) our cash Gross Profit is being battered. The problem has been exacerbated by the recent boom time where Channel 4's *You Are What You Eat* caused demand to increase staffing and salaries only to become "you are what you ate" as sales did not last. Not everyone reduced the wage bill to compensate.

Market experts continue to forecast static sales for high street "bricks and mortar" retailers and some analysts predict another quarter per cent interest rate rise in February. The only factor all analysts agree on is that overheads will continue to rise. In this bureaucratic and business-unfriendly country that prediction, at least, can be taken to the bank.

To gain control of salaries, refer to a previous strong performing year and evaluate the percentage wages bill against turnover. Now calculate the existing wage percentage using the most recent three-month figures. Most will show a higher cost today.

Complete a weekly rota in spreadsheet form that shows the days of the week across the top and defines the individual staff positions required down the side. Against each position enter the necessary shift times and hours under the relevant day.

Total the hours each day and at the end of the week for each position. You now have a weekly schedule of essential hours. Adding rates of pay complete with Tax and NI produces a weekly financial cost.

Calculate this projected cost against present sales and tweak the schedule until the percentage gets back in line with that previous peak-performing year or a new target you decide.

Compare this template to a similar sheet that records the actual staff situation now. Reduce the cost by working with staff to agree new shifts or as they leave employment alter recruitment to match the template. By using a percentage figure against sales as a guide, Gross Profit is protected from a sudden rise in operating costs.

Gross Profit (GP) percentage

This is the factor that determines whether all the hard work to obtain sales will actually pay for the cost of running the business and return net profit.

GP stated in cash form is the difference between sales and the cost of sales (products) for a given period. For example, a shop that turns over £400,000 might have purchases of £260,000, producing a cash GP of £140,000. This GP can then be expressed in percentage terms by taking the cost of sales figure from the turnover and dividing it by the turnover x 100 (£400,000 – £260,000/£400,000 x 100 = 35 per cent.

Since that £140,000 of GP will pay for the overheads and net profit it is crucial to maintain the GP percentage, in this case, 35 per cent.

The really frightening thing about GP is that the slightest loss of percentage can have a devastating effect. A 1 per cent loss in this example of £400,000 turnover is £4,000 cash profit gone. Unfortunately, discounting, wastage, theft and poor ordering discipline can easily and negatively influence GP.

Discounts reduce sales revenue; increasing wastage means more products are bought but no more revenue is gleaned (as with theft) and poor ordering results in product not being purchased from the cheapest source. Retailers should evaluate and instigate controls on each of these factors to protect shop profitability.

Sales

Without sales, any good work on wages and GP is immaterial and vice versa. It is predicted that only the smartest retailers will see growth this year while those that keep doing what they have always done will suffer steady decline.

Being smart means stocking and attractively merchandising products that the consumer wants at competitive prices. Some independent retailers are guilty of displaying a product selection that reflects their own taste rather than that of changing consumer demand.

Other retailers offer a dated selection purely because they cannot find the time to alter it. If you do not have the products that the local shopper is looking for why would they visit? Attend our industry's trade shows, read the trade press, talk to colleagues and keep abreast of trends.

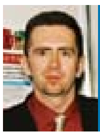
Present an abundant image by constantly pulling forward the stock on shelves, fill gaps, make sure that the storeroom is not packed with lines that should be on the shop floor and if cash flow permits, pack every inch of your retail space with items for sale. The floor space is costing money to rent and operate so fill it up!

Another classic error is to promote lines that a retailer wants to be rid of but if they have not sold at normal price it is because nobody wants them. Why would customers find a promotion on items nobody wants enticing? Rotate and promote the best-selling products to provide a stimulating shopping experience.

Strategically, sales can only be enlarged in three ways; by increasing the number of customers or the number of times a current customer visits the shop and by augmenting the amount they spend. Every decision a retailer makes must influence one or more of these factors to have a positive effect on sales growth.

Summary

Review the projects being worked on for 2007. If they don't directly influence one of these three key performance generators think carefully about their worth. 2006 was a rollercoaster of sales fluctuations; by planning for 2007 we can ensure stability and perhaps respectable growth. HFB



If you have any questions for Talking Shop or would like further information on Stuart Jackson's consultancy service, contact him on 0131 315 0303 or email stuart@forceofnature.co.uk or visit www.forceofnature.co.uk