



HOW TO SUCCEED IN BUSINESS IN FOUR EASY STEPS

STEP 1: Get a grip on your emotions and decide on your goals.

Ask Norm Brodsky the single most important piece of advice he gives to people starting a business, and he'll talk about preserving capital and maintaining gross-profit margins. "But I don't begin with that. I begin by asking them their goals.

"The truth, of course, is that the initial goal of every business is to survive long enough to see whether or not the business is viable. I don't care what business you're talking about or how much capital you have. You never know for sure if a business is viable until you do it in the real world. But viability is just a step on the way to somewhere else, and I want to know where some-

where else is. I want to hear what people have to say. What I'm listening for are goals that can't be achieved by business. Or goals that will get in the way of a business. Or goals that are totally unrealistic given the particular business they're looking at. I'm listening for what's really motivating people."

STEP 2: Make sure you understand what cash flow is and where it's going to come from.

"Everybody is scared going into their first business," says Brodsky, "everybody with any sense, that is. That's one reason you need a business plan. It helps to demystify the process. It

takes some of the emotion out of the situation.”

People starting their first business “confuse cash flow with sales or with having money in the bank. They believe that to be successful, all you have to do is generate sales. In fact, what you need is the right kind of sales. The wrong kind can drive you straight into bankruptcy.

“To avoid that, you have to realize, first, that your capital is limited. I don't care who you are. Nobody starts a business with unlimited capital, not even IBM. So the whole idea is to make sure, number one, that you have enough capital to begin with, and number two, that it will last long enough to determine whether or not the business is viable. By viability, I mean the point at which the business is generating internally the cash it needs to pay its bills. It can survive on its own. A business plan is essentially your best guess as to how you're going to get there.

“Now, understand, when I say business plan, I don't mean anything elaborate. What I'm talking about is a modified income statement and cash-flow statement, real simple. I just want a reasonable expectation of sales by month for a year.

“Once you have reasonable sales projections, you can break them down by product category and calculate the cost of goods sold [COGS], or, in service businesses, the cost of sales. You subtract COGS from sales, and you have your gross profit or—expressed as a percentage of sales—your gross margin. In my opinion, gross profit is the single most important number in any new business. It determines everything else about your business—the amount of capital you need, the volume of sales, the overhead you can afford, the time it will take to determine viability, even viability itself.

“Say you're selling an item for \$1 that costs you 90¢ to produce or to buy. Your gross profit is 10¢ per item, or 10% of sales. Suppose you need \$5,000 per month to cover your overhead. To get it, you have to do \$50,000 per month in sales. Now, let's say it takes you three months to collect your receivables. You'd have to put up more than \$100,000 in cash to get the \$5,000 per month you need to break even. That's usually not a viable business.

“And gross profit is the linchpin, the deciding factor. You have to pay all your expenses out of gross profit—your salary, your rent, the phone bill, gas, electricity, photocopying, whatever. If your gross margin is 10%, you need \$10 in sales for every \$1 of expenses just to break even. If your gross margin is 40%, you need only \$2.50 in sales for every \$1 of expenses. That difference is crucial when you're working with limited capital. The higher your gross margin, the fewer sales you need to cover expenses, and the longer your capital will last. And, for most start-ups, time is survival.”

Here, in Brodsky's opinion, are the two most important rules for every new business:

1 Protect your capital. Spend it only on things you are certain will generate positive cash flow in the short term.

2 Maintain the highest monthly gross-profit margin you are capable of achieving. It's important to go after high-margin customers, which generally means smaller-volume customers.

STEP 3: Recognize the sales mentality before it's too late.

There are times, Brodsky says, when he thinks it's a miracle that anyone starting out fresh manages to stay in business. “You make so many mistakes. You get no good advice. It's so easy to get off on the wrong track.

“Take the salesman's mentality, which almost all entrepreneurs have when they first go into business. They want to see sales go up every month, every day, every hour. I myself didn't care about anything except our weekly sales figures. My investors were the same way, and many of them were accountants. You think they ever asked me about profits? All they wanted to know about were sales.

“That's the sales mentality. It's the idea that you should focus all your attention on making sales. With established companies, everybody talks about earnings, past and future, but with new companies, it's all sales. It's very dangerous, especially if you're operating out of your basement on a shoestring, says Brodsky.

“Look. It all goes back to the fundamental reality that you are working with limited capital. If your gross profit is not enough to cover your expenses, you have to dip into your capital to make up the difference. You dip too much, and pretty soon you run out.

“Spend your time developing relationships with your highest-margin customers. Let the low-margin customers come to you, and then negotiate the price up.

“The sales mentality gets in the way of the real goal by substituting a short-term goal, making a sales target, for the long-term one: determining viability. What if you have a series of bad months? Those results could be telling you something—that the business isn't viable, or that you're not capable of selling at a high enough gross margin to achieve your goal.

If your business is viable, and if it survives, it will eventually reach what I call critical mass, and when it does your whole situation will change.

“The usual alternative is to delude yourself with a series of high-volume, low-margin months. It's easy. You just drop your price below your competitors', and you can make all the sales you want. You'll think you're doing fine. You won't run out of cash as long as your sales keep rising and you can collect before you pay. Trouble is, you also have more payables than you can handle. You're bankrupt, and you don't know it. All of a sudden, you hit a couple of bad months, your cash disappears, and you lose everything. It happens all the time.

“The way to avoid that fate is to stay focused on your real goal, to follow the rules and watch the numbers. If you watch closely enough, a picture begins to emerge. The picture gets clearer, until you realize that you're going to make it—or that it's time to try something else.”

STEP 4: Learn to anticipate and recognize the changes in your business.

Norm Brodsky says he has learned over the years that it's a big mistake to let yourself get too relaxed in business—to ever start thinking you're out of the woods and safe and secure. “I'm not just talking about start-ups here. I mean companies of any size, at any stage of development. Because fundamental shifts occur in business, and they can be good or bad.” Businesses may change, he says, “because their customers develop different needs or because they start selling to another type of customer or because a new competitor enters the market. There could be dozens of reasons. But those changes occur, and you may not be aware of them at first. They are often hidden. If the changes are bad, and you're not on top of them quickly enough, they can destroy you.

“If your business is viable, and if it survives, it will eventually reach what I call critical mass, and when it does your whole situation will change. Because critical mass is a threshold, a very significant one. It usually depends on some key factor in your business hitting a certain level. The factor may be the size of your customer base. It may be the number

of active accounts you have. There are probably 10 different types of critical mass. But however many variations there are, they all translate into the same thing for every business: break-even cash flow. I don't mean breakeven on a profit-and-loss basis. I'm talking about getting to where the cash you generate each month is enough to sustain the business and allow it to grow without your having to go outside for new investment.

“That is the major turning point for any new venture. Before critical mass, a business is a fledgling enterprise surviving on external capital. It still has its umbilical cord. After critical mass, the business is a freestanding, self-sustaining entity capable of making its own way in the world. It's your next goal after you determine viability. The challenge is to figure out where the goal line is.

“After critical mass, growing the business becomes a matter of choice. That is clearly a huge change from before—a predictable one, and a good one, but a change that has major consequences. It opens up a whole world of possibilities that you couldn't even think about during the start-up phase.

“As long as you're surviving on external capital you really have to focus on building the business you started to build. You have to be very careful, for instance, about experimenting with new products or services, at least until you've expanded your basic business as far as it can go. You can't afford to experiment. You don't have the time or the money.” You have to do everything you can, Brodsky reminds, to reach viability before your capital runs out.

“After critical mass, you're living off your own internally generated cash. You have profits to put in the bank. You may decide you want to invest some of them back in the business, and I think you should. It's important to explore new avenues, especially if you have a strong customer base. You might even take on some additional debt, which you can pay off out of profits. Yes, it's a little more risky, but you have the luxury to take more risks, to try some experiments, because you're playing with your own money. If you invest intelligently, you have the chance to help yourself and your customers and strengthen the business. And because you've reached critical mass, you can take the chance without putting the business in jeopardy.”

Brodsky advises, “In business, you have to try to be objective, to be as clear as possible about what you're doing and why, and about what the likely consequences will be. You can use the tools of business to help you do that, to help you gain perspective. In the end, you may decide to go with your emotions anyway, but at least it's a choice.” ■ *Bo Burlingham*