

# Simple Numbers 2.0 The Profit Cube

by  
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FOREWORD BY **VERNE HARNISH**, CEO, GAZELLES, INC.  
AUTHOR, *MASTERING THE ROCKEFELLER HABITS*

**SIMPLE  
NUMBERS,  
STRAIGHT TALK,  
BIG** 4 KEYS TO UNLOCK YOUR  
BUSINESS POTENTIAL  
**PROFITS!**

**GREG CRABTREE**

WITH BEVERLY BLAIR HARZOG

Simple Numbers... Straight Talk... Big Profits  
*4 Keys to Unlock Your Business Potential*

- **Eliminate Distortion - Your data is lying! - The way you deal with Owner's compensation and Revenue is distorting your data.**
- **Set Profit Targets** - Profit matters more than you think – How to set the right profit targets for your business
- **Get Profitable** - Labor Productivity drives your profit engine – How to measure it and improve it
- **Cash Strategy** - 4 Forces of cash flow – Get the priorities right to set your business on a solid foundation



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# Distortion #1

## Why Owner Salaries Matter

- You get
  - a salary for what you do and
  - a return on what you own
- Why Your Net Income is lying!
- Be a More Demanding Employee
- Be a More Demanding Shareholder
- Can distort profits from start up to over \$60 million in revenue



# Distortion #1

## Why Owner Salaries Matter

Time for the survey!



## Distortion #2

### Finance terminology – Watch your language!

Weak

- **Revenue** – This is the vanity number

Better

- **Gross profit** – Revenue less direct costs (the true economic engine) – my definition excludes labor

Best

- **Contribution margin** – my definition is gross profit minus direct labor

Weak

- **EBITDA** - Earnings before: Interest, Taxes, Depreciation and Amortization – the most abused term in finance

Best

- **Pre-tax profits** – easier to define and more traceable to true cash flow





## The Crabtree P&L Model

	Construction Company	Services Company
Revenue	<u>\$20,000,000</u>	<u>\$3,750,000</u>
Cost of Goods Sold:		
Materials	5,000,000	-
Subcontractors	<u>12,150,000</u>	<u>900,000</u>
Total Cost of Goods Sold	<u>17,150,000</u>	<u>900,000</u>
<b>Gross Profit</b>	2,850,000	2,850,000
Direct Labor	<u>1,000,000</u>	<u>1,000,000</u>
<i>Direct LER (GP/DL)</i>	2.85	2.85
<b>Contribution Margin</b>	<u>1,850,000</u>	<u>1,850,000</u>
Operating expenses:		
Facilities	150,000	150,000
Marketing	75,000	75,000
Salaries (management and admin)	750,000	750,000
Payroll taxes and benefits	100,000	100,000
Other operating expenses	<u>150,000</u>	<u>150,000</u>
Total operating expenses	<u>1,225,000</u>	<u>1,225,000</u>
<i>Management LER (CM/Mgmt Labor)</i>	<u>2.46</u>	<u>2.46</u>
<b>Net operating Income</b>	<u>625,000</u>	<u>625,000</u>
<b>Overall LER</b>	<u>1.63</u>	<u>1.63</u>
Other expenses:		
Depreciation	75,000	75,000
Interest Expense	<u>25,000</u>	<u>25,000</u>
Total other expenses	<u>100,000</u>	<u>100,000</u>
<b>Pre-tax Net Income</b>	<u>\$525,000</u>	<u>\$525,000</u>
<i>as a % of Revenue</i>	2.63%	14.00%
<i>as a % of Gross Profit</i>	18.42%	18.42%

**The Crabtree P&L Model**

	Construction Company	Services Company		
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**Does your engine fit the frame it is trying to move?**

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**Does your engine fit the frame it is trying to move?**

# Breaking Even Isn't Good Enough Why 10% is the New Breakeven

## Profitability Percentages (Pre-Tax):

5% - You're on Life Support

10% - When you're a *good* business

15% - When you're a *great* business

- Anything over 15%, take it while you can!

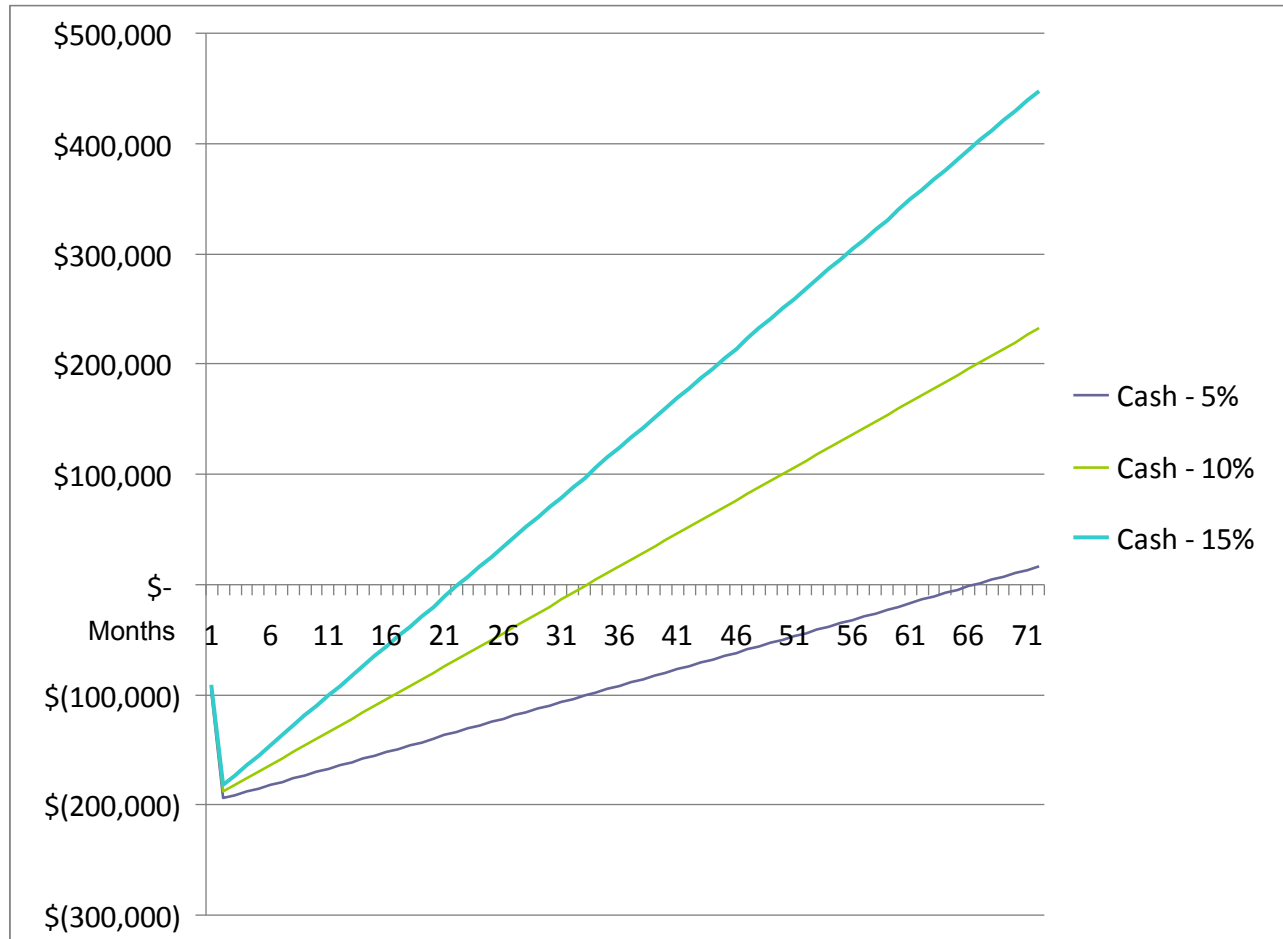


# Cash Flow versus Profit

- Why profit matters more than you think!
  - Examples at 5%, 10% & 15%
  - Revenue at \$100,000 per month
  - Tax Rate 40%
  - Assume service-based business that bills at the end of the month and gets paid in an average of 45 days



# Cash Flow versus Profit Recap





# What is Your Profit Level?

1. Growing Profitably (growth  $>5\%$  and net profit  $>10\%$ )
2. Profitably Stable (growth  $\pm 5\%$  and net profit  $>10\%$ )
3. Need to cut unproductive costs (Profits  $>0\% <10\%$ )
4. Stage 1 Denial; I can grow into my costs (Profits  $>0\% <10\%$ )
5. Stage 2 Denial; Consuming Muscle (Profits  $<0\%$ )



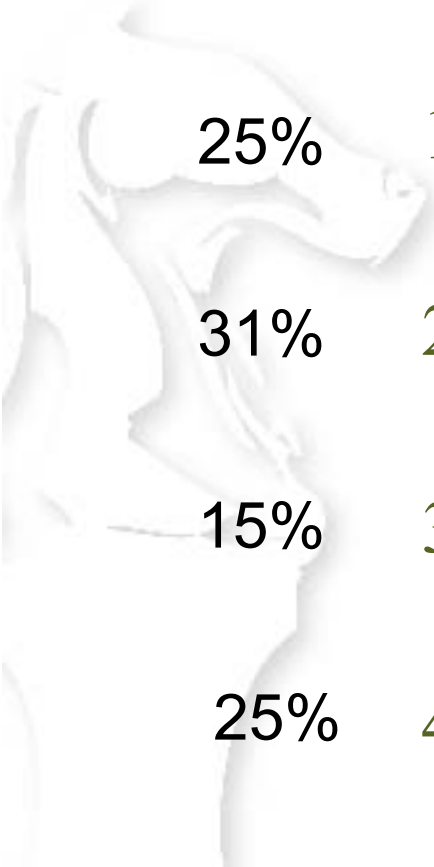
# What is Your Profit Level?

Time for the survey!



# What is Your Profit Level?

## – Client Results

- 
- 25% 1. Growing Profitably (growth  $>5\%$  and net profit  $>10\%$ )
  - 31% 2. Profitably Stable (growth  $\pm 5\%$  and net profit  $>10\%$ )
  - 15% 3. Need to cut unproductive costs (Profits  $>0\% <10\%$ )
  - 25% 4. Stage 1 Denial; I can grow into my costs (Profits  $>0\% <10\%$ )
  - 4% 5. Stage 2 Denial; Consuming Muscle (Profits  $<0\%$ )



# Key Characteristic Between Top 2 Groups

- Growing Profitably Key Characteristic?



# Key Characteristic Between Top 2 Groups

- Growing Profitably Key Characteristic?
  - CEO is Sales & Marketing focused



# Key Characteristic Between Top 2 Groups

- Growing Profitably Key Characteristic?
  - CEO is Sales & Marketing focused
- Profitably Stable Key Characteristic?



# Key Characteristic Between Top 2 Groups

- Growing Profitably Key Characteristic?
  - CEO is Sales & Marketing focused
- Profitably Stable Key Characteristic?
  - CEO is Operations focused



# Labor Efficiency Ratio (LER) By Company

- Company-wide example of an underperforming business
- Watch for LER movement across time





# The Road to 15% Pre-Tax Profit

- Know your current labor model
- Hold labor dollars constant while driving to profitability
- Holding labor dollars constant does not mean you can't change staff
- Use the “baffle” concept to grow to 15% in profit before you add more labor



	Original
Revenue	450,000.00
Direct Costs excluding labor	<u>130,000.00</u>
Gross Profit	320,000.00 71.1%
Direct Labor	<u>90,000.00</u>
Contribution Margin	<u>230,000.00</u>
Management/Admin Labor	75,000.00
Sales Labor	35,000.00
Other Operating Costs	<u>100,000.00</u>
Pre-tax Profit	<u><u>20,000.00</u></u>
Pre-tax Profit as % of Revenue	4.44%
CM as % of Revenue	51.11%
Other Operating Costs as % of Rev	22.22%
Labor Efficiency:	
Direct Labor (GP/DL)	\$3.56
Sales Labor (CM/SL)	\$6.57
Management Labor (CM/ML)	\$3.07

	Original	Step #1 10%
Revenue	450,000.00	492,195.19
Direct Costs excluding labor	<u>130,000.00</u>	<u>142,195.19</u>
Gross Profit	320,000.00 71.1%	350,000.00 71.1%
Direct Labor	<u>90,000.00</u>	<u>90,000.00</u>
Contribution Margin	<u>230,000.00</u>	<u>260,000.00</u>
Management/Admin Labor	75,000.00	75,000.00
Sales Labor	35,000.00	35,000.00
Other Operating Costs	<u>100,000.00</u>	<u>100,000.00</u>
Pre-tax Profit	<u>20,000.00</u>	<u>50,000.00</u>
Pre-tax Profit as % of Revenue	4.44%	10.16%
CM as % of Revenue	51.11%	52.82%
Other Operating Costs as % of Rev	22.22%	20.32%
Labor Efficiency:		
Direct Labor (GP/DL)	\$3.56	\$3.89
Sales Labor (CM/SL)	\$6.57	\$7.43
Management Labor (CM/ML)	\$3.07	\$3.47

	Original	Step #1 10%	Step #2 15%
Revenue	450,000.00	492,195.19	534,383.35
Direct Costs excluding labor	<u>130,000.00</u>	<u>142,195.19</u>	<u>154,383.35</u>
Gross Profit	320,000.00 71.1%	350,000.00 71.1%	380,000.00 71.1%
Direct Labor	<u>90,000.00</u>	<u>90,000.00</u>	<u>90,000.00</u>
Contribution Margin	<u>230,000.00</u>	<u>260,000.00</u>	<u>290,000.00</u>
Management/Admin Labor	75,000.00	75,000.00	75,000.00
Sales Labor	35,000.00	35,000.00	35,000.00
Other Operating Costs	<u>100,000.00</u>	<u>100,000.00</u>	<u>100,000.00</u>
Pre-tax Profit	<u>20,000.00</u>	<u>50,000.00</u>	<u>80,000.00</u>
Pre-tax Profit as % of Revenue	4.44%	10.16%	14.97%
CM as % of Revenue	51.11%	52.82%	54.27%
Other Operating Costs as % of Rev	22.22%	20.32%	18.71%
Labor Efficiency:			
Direct Labor (GP/DL)	\$3.56	\$3.89	\$4.22
Sales Labor (CM/SL)	\$6.57	\$7.43	\$8.29
Management Labor (CM/ML)	\$3.07	\$3.47	\$3.87

	Original	Step #1 10%	Step #2 15%	Step #3 back to 10%
Revenue	450,000.00	492,195.19	534,383.35	534,383.35
Direct Costs excluding labor	<u>130,000.00</u>	<u>142,195.19</u>	<u>154,383.35</u>	<u>154,383.35</u>
Gross Profit	320,000.00 71.1%	350,000.00 71.1%	380,000.00 71.1%	380,000.00 71.1%
Direct Labor	<u>90,000.00</u>	<u>90,000.00</u>	<u>90,000.00</u>	<u>98,333.33</u>
Contribution Margin	230,000.00	260,000.00	290,000.00	281,666.67
Management/Admin Labor	75,000.00	75,000.00	75,000.00	83,333.33
Sales Labor	35,000.00	35,000.00	35,000.00	43,333.33
Other Operating Costs	<u>100,000.00</u>	<u>100,000.00</u>	<u>100,000.00</u>	<u>101,666.67</u>
Pre-tax Profit	<u>20,000.00</u>	<u>50,000.00</u>	<u>80,000.00</u>	<u>53,333.33</u>
Pre-tax Profit as % of Revenue	4.44%	10.16%	14.97%	9.98%
CM as % of Revenue	51.11%	52.82%	54.27%	52.71%
Other Operating Costs as % of Rev	22.22%	20.32%	18.71%	19.03%
Labor Efficiency:				
Direct Labor (GP/DL)	\$3.56	\$3.89	\$4.22	\$3.86
Sales Labor (CM/SL)	\$6.57	\$7.43	\$8.29	\$6.50
Management Labor (CM/ML)	\$3.07	\$3.47	\$3.87	\$3.38

	Original	Step #1 10%	Step #2 15%	Step #3 back to 10%	Step #4 back to 15%
Revenue	450,000.00	492,195.19	534,383.35	534,383.35	587,821.68
Direct Costs excluding labor	<u>130,000.00</u>	<u>142,195.19</u>	<u>154,383.35</u>	<u>154,383.35</u>	<u>169,821.68</u>
Gross Profit	320,000.00 71.1%	350,000.00 71.1%	380,000.00 71.1%	380,000.00 71.1%	418,000.00 71.1%
Direct Labor	<u>90,000.00</u>	<u>90,000.00</u>	<u>90,000.00</u>	<u>98,333.33</u>	<u>98,333.33</u>
Contribution Margin	230,000.00	260,000.00	290,000.00	281,666.67	319,666.67
Management/Admin Labor	75,000.00	75,000.00	75,000.00	83,333.33	83,333.33
Sales Labor	35,000.00	35,000.00	35,000.00	43,333.33	43,333.33
Other Operating Costs	<u>100,000.00</u>	<u>100,000.00</u>	<u>100,000.00</u>	<u>101,666.67</u>	<u>105,000.00</u>
Pre-tax Profit	<u>20,000.00</u>	<u>50,000.00</u>	<u>80,000.00</u>	<u>53,333.33</u>	<u>88,000.00</u>
Pre-tax Profit as % of Revenue	4.44%	10.16%	14.97%	9.98%	14.97%
CM as % of Revenue	51.11%	52.82%	54.27%	52.71%	54.38%
Other Operating Costs as % of Rev	22.22%	20.32%	18.71%	19.03%	17.86%
Labor Efficiency:					
Direct Labor (GP/DL)	\$3.56	\$3.89	\$4.22	\$3.86	\$4.25
Sales Labor (CM/SL)	\$6.57	\$7.43	\$8.29	\$6.50	\$7.38
Management Labor (CM/ML)	\$3.07	\$3.47	\$3.87	\$3.38	\$3.84

**Thinking model**

	<b>Actual</b>	<b>Change</b>	<b>Target</b>
Revenue	6,234,494.04	1,122,567.98	7,357,062.02
Non Labor Direct costs	815,714.64		962,590.25
<b>Gross Profit</b>	5,418,779.40		6,394,471.77
<i>as % to Sales</i>	86.92%		86.92%
Direct Labor	1,980,924.25	356,863.52	2,337,787.77
<b>Contribution Margin</b>	3,437,855.15		4,056,684.00
<i>as % to Sales</i>	55.14%		55.14%
<i>Direct LER</i>	2.74		2.74
<b>Operating Expenses:</b>			
Facilities	370,655.12		370,655.12
Marketing	199,181.28		235,045.38
Management Labor	1,104,400.00	200,000.00	1,304,400.00
Payroll taxes & benefits	230,607.08		272,368.59
Other operating expenses	819,406.72		966,947.12
<b>Total Operating Expenses</b>	2,724,250.20		3,149,416.22
<i>as % to Sales</i>	43.70%		42.81%
<i>Management LER</i>	3.11		3.11
<b>Net Operating Income</b>	713,604.95		907,267.78
<i>as % to Sales</i>	11.45%		12.33%
Marketing as % of Revenue	3.19%		3.19%
PR Taxes & Benefits as % of All Labor	20.88%		20.88%
Other Operating Expenses as % of Revenue	13.14%		13.14%

# Adding \$200k Labor Recap

## Adding \$200,000 of Management Labor

- Requires \$1.1M increase in revenue!
  - Assumes you maintain Direct LER
  - Assumes you maintain Management LER
- To produce less forces you to pay for wage increase out of YOUR PROFITS!





# 4 Forces of Cash Flow

## Prioritized In Order:

- Taxes
- Repay debt
- Build Working Capital (Core Capital Target)
- Dividends (Distributions)



# Labor Efficiency Ratio by Division

- Landscaping Business with 4 Divisions
- Drill Down on Turf Division



	<b>TOTAL</b>	<b>Irrigation</b>	<b>Landscape</b>	<b>Snow</b>	<b>Turf</b>	
Revenue	10,615,483.28	3,095,230.08	2,589,640.76	1,792,433.28	3,138,179.16	
COGS	3,107,190.44	809,436.08	788,253.16	690,436.44	819,064.76	
Gross Profit	7,508,292.84	2,285,794.00	1,801,387.60	1,101,996.84	2,319,114.40	
	<b>GP%</b>	<b>70.73%</b>	<b>73.85%</b>	<b>61.48%</b>	<b>73.90%</b>	
Direct Labor	1,871,249.08	564,850.36	416,542.28	285,192.56	604,663.88	
Contribution Margin	5,637,043.76	1,720,943.64	1,384,845.32	816,804.28	1,714,450.52	
	<b>Direct LER</b>	<b>\$ 4.01</b>	<b>\$ 4.05</b>	<b>\$ 4.32</b>	<b>\$ 3.86</b>	<b>\$ 3.84</b>
Management Labor	724,663.56	163,196.80	200,336.36	158,262.40	202,868.00	
	<b>Mgmt LER</b>	<b>\$ 7.78</b>	<b>\$ 10.55</b>	<b>\$ 6.91</b>	<b>\$ 5.16</b>	<b>\$ 8.45</b>
Net Division income	4,912,380.20	1,557,746.84	1,184,508.96	658,541.88	1,511,582.52	
	<b>As % of Revenue</b>	<b>46.28%</b>	<b>50.33%</b>	<b>45.74%</b>	<b>36.74%</b>	<b>48.17%</b>
	<b>As % of GP</b>	<b>65.43%</b>	<b>68.15%</b>	<b>65.76%</b>	<b>59.76%</b>	<b>65.18%</b>
Corporate Labor	750,000.00					
Other Opex	3,110,336.44					
Net income	1,052,043.76					
	<b>As % of Revenue</b>	<b>9.91%</b>				
	<b>As % of GP</b>	<b>14.01%</b>				
<b>Corporate LER</b>	<b>\$ 6.55</b>					

	<b>TOTAL</b>	<b>Irrigation</b>	<b>Landscape</b>	<b>Snow</b>	<b>Turf</b>	
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<b>Corporate LER</b>	<b>\$ 6.55</b>				

Best  
Worst

Turf Division

	2011	2012	Diff
Revenue	3,326,469.91	3,138,179.16	(188,290.75)
COGS	877,982.16		
Gross Profit	2,448,487.75		
	<b>GP%</b>	<b>73.61%</b>	
Direct Labor	755,829.85		
Contribution Margin	1,692,657.90		
	<b>Direct LER \$</b>	<b>3.24</b>	
Management Labor	213,011.40		
	<b>Mgmt LER \$</b>	<b>7.95</b>	
Net Division income	1,479,646.50		
	<b>As % of Revenue</b>	<b>44.48%</b>	
	<b>As % of GP</b>	<b>60.43%</b>	

What happens when you cut to grow?

Turf Division

	2011	2012	Diff
Revenue	3,326,469.91	3,138,179.16	(188,290.75)
COGS	877,982.16	819,064.76	
Gross Profit	2,448,487.75	2,319,114.40	(129,373.35)
	<b>GP%</b>	<b>73.61%</b>	<b>73.90%</b>
Direct Labor	755,829.85	604,663.88	(151,165.97)
Contribution Margin	1,692,657.90	1,714,450.52	21,792.62
	<b>Direct LER \$</b>	<b>3.24</b>	<b>\$ 3.84</b>
Management Labor	213,011.40	202,868.00	(10,143.40)
	<b>Mgmt LER \$</b>	<b>7.95</b>	<b>\$ 8.45</b>
Net Division income	1,479,646.50	1,511,582.52	31,936.02
	<b>As % of Revenue</b>	<b>44.48%</b>	<b>48.17%</b>
	<b>As % of GP</b>	<b>60.43%</b>	<b>65.18%</b>

Great example of when a decline can be an increase!

# Labor Efficiency Ratio by Location

- Multi-location Business
- Largest versus smallest
- Likely pattern for growth
- Company-wide what-if model



**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue	10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales	2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>	7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
Direct Labor	3,506,405.74	1,914,299.93	629,067.51	188,096.10	774,942.19	-
<b>Contribution Margin (CM)</b>	4,086,638.60	2,019,983.35	960,472.80	311,074.76	795,107.69	-
<i>as % to Sales</i>	39.47%	37.26%	46.92%	55.20%	34.25%	
<i>Direct LER</i>	2.17	2.06	2.53	2.65	2.03	
<b>Corporate Expenses:</b>						
Management Labor	1,369,976.41	435,352.00	260,978.00	90,012.00	155,789.00	427,845.41
Payroll taxes & benefits	1,047,581.08	414,040.96	234,194.81	77,191.73	240,762.41	81,391.18
Other operating expenses	865,267.08	342,383.78	147,346.10	33,952.29	142,323.60	199,261.31
<b>Total Operating Expenses</b>	3,282,824.57	1,191,776.74	642,518.90	201,156.02	538,875.01	708,497.89
<i>as % to Sales</i>	31.71%	21.98%	31.39%	35.69%	23.21%	
<i>Management LER to CM</i>	2.98	4.64	3.68	3.46	5.10	
<b>Net Operating Income</b>	803,814.03	828,206.61	317,953.90	109,918.74	256,232.68	(708,497.89)
<i>as % to Sales</i>	7.76%	15.28%	15.53%	19.50%	11.04%	
<i>as % to GP</i>	10.59%	21.05%	20.00%	22.02%	16.32%	
<b>Other Income (Expense):</b>						
Interest expense	(139,854.66)	(74,597.62)	(3,367.63)	(20,169.05)	(11,458.28)	(30,262.07)
Depreciation	(320,237.01)	(215,058.31)	(17,158.71)	(20,477.47)	(57,090.62)	(10,451.89)
Other income	892.51	-	-	-	-	892.51
<b>Total Other Income (Expense)</b>	(459,199.16)	(289,655.94)	(20,526.34)	(40,646.52)	(68,548.91)	(39,821.46)
<b>Net Income</b>	344,614.87	538,550.67	297,427.56	69,272.22	187,683.77	(748,319.35)
<i>as % to Sales</i>	3.33%	9.93%	14.53%	12.29%	8.08%	
Corporate LER (All CM per Corp Labor)	9.55					

**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue	10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales	2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>	7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
Direct Labor	3,506,405.74	1,914,299.93	629,067.51	188,096.10	774,942.19	-
<b>Contribution Margin (CM)</b>	4,086,638.60	2,019,983.35	960,472.80	311,074.76	795,107.69	-
<i>as % to Sales</i>	39.47%	37.26%	46.92%	55.20%	34.25%	
<i>Direct LER</i>	2.17	2.06	2.53	2.65	2.03	
<b>Corporate Expenses:</b>						
Management Labor	1,369,976.41	435,352.00	260,978.00	90,012.00	155,789.00	427,845.41
Payroll taxes & benefits	1,047,581.08	414,040.96	234,194.81	77,191.73	240,762.41	81,391.18
Other operating expenses	865,267.08	342,383.78	147,346.10	33,952.29	142,323.60	199,261.31
<b>Total Operating Expenses</b>	3,282,824.57	1,191,776.74	642,518.90	201,156.02	538,875.01	708,497.89
<i>as % to Sales</i>	31.71%	21.98%	31.39%	35.69%	23.21%	
<i>Management LER to CM</i>	2.98	4.64	3.68	3.46	5.10	-
<b>Net Operating Income</b>	803,814.03	828,206.61	317,953.90	109,918.74	256,232.68	(708,497.89)
<i>as % to Sales</i>	7.76%	15.28%	15.53%	19.50%	11.04%	
<i>as % to GP</i>	10.59%	21.05%	20.00%	22.02%	16.32%	
<b>Other Income (Expense):</b>						
Interest expense	(139,854.66)	(74,597.62)	(3,367.63)	(20,169.05)	(11,458.28)	(30,262.07)
Depreciation	(320,237.01)	(215,058.31)	(17,158.71)	(20,477.47)	(57,090.62)	(10,451.89)
Other income	892.51	-	-	-	-	892.51
<b>Total Other Income (Expense)</b>	(459,199.16)	(289,655.94)	(20,526.34)	(40,646.52)	(68,548.91)	(39,821.46)
<b>Net Income</b>	344,614.87	538,550.67	297,427.56	69,272.22	187,683.77	(748,319.35)
<i>as % to Sales</i>	3.33%	9.93%	14.53%	12.29%	8.08%	
Corporate LER (All CM per Corp Labor)	9.55					

**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue	10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales	2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>	7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
Direct Labor	3,506,405.74	1,914,299.93	629,067.51	188,096.10	774,942.19	-
<b>Contribution Margin (CM)</b>	4,086,638.60	2,019,983.35	960,472.80	311,074.76	795,107.69	-
<i>as % to Sales</i>	39.47%	37.26%	46.92%	55.20%	34.25%	
<i>Direct LER</i>	2.17	2.06	2.53	2.65	2.03	
<b>Corporate Expenses:</b>						
Management Labor	1,369,976.41	435,352.00	260,978.00	90,012.00	155,789.00	427,845.41
Payroll taxes & benefits	1,047,581.08	414,040.96	234,194.81	77,191.73	240,762.41	81,391.18
Other operating expenses	865,267.08	342,383.78	147,346.10	33,952.29	142,323.60	199,261.31
<b>Total Operating Expenses</b>	3,282,824.57	1,191,776.74	642,518.90	201,156.02	538,875.01	708,497.89
<i>as % to Sales</i>	31.71%	21.98%	31.39%	35.69%	23.21%	
<i>Management LER to CM</i>	2.98	4.64	3.68	3.46	5.10	-
<b>Net Operating Income</b>	803,814.03	828,206.61	317,953.90	109,918.74	256,232.68	(708,497.89)
<i>as % to Sales</i>	7.76%	15.28%	15.53%	19.50%	11.04%	
<i>as % to GP</i>	10.59%	21.05%	20.00%	22.02%	16.32%	
<b>Other Income (Expense):</b>						
Interest expense	(139,854.66)	(74,597.62)	(3,367.63)	(20,169.05)	(11,458.28)	(30,262.07)
Depreciation	(320,237.01)	(215,058.31)	(17,158.71)	(20,477.47)	(57,090.62)	(10,451.89)
Other income	892.51	-	-	-	-	892.51
<b>Total Other Income (Expense)</b>	(459,199.16)	(289,655.94)	(20,526.34)	(40,646.52)	(68,548.91)	(39,821.46)
<b>Net Income</b>	344,614.87	538,550.67	297,427.56	69,272.22	187,683.77	(748,319.35)
<i>as % to Sales</i>	3.33%	9.93%	14.53%	12.29%	8.08%	
Corporate LER (All CM per Corp Labor)	9.55					

**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue	10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales	2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>	7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
Direct Labor	3,506,405.74	1,914,299.93	629,067.51	188,096.10	774,942.19	-
<b>Contribution Margin (CM)</b>	4,086,638.60	2,019,983.35	960,472.80	311,074.76	795,107.69	-
<i>as % to Sales</i>	39.47%	37.26%	46.92%	55.20%	34.25%	
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<i>Management LER to CM</i>	2.98	4.64	3.68	3.46	5.10	-
<b>Net Operating Income</b>	803,814.03	828,206.61	317,953.90	109,918.74	256,232.68	(708,497.89)
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Corporate LER (All CM per Corp Labor)	9.55					



**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue	10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales	2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>	7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
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**LER Calculation by Location**

**2012**

	Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
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**2012**

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<i>as % to Sales</i>	3.33%	9.93%	14.53%	12.29%	8.08%	

Corporate LER (All CM per Corp Labor) **9.55**

<b>LER Calculation by Location</b>		<b>2012</b>					
		Best	Worst				
		Total Company	Location 1	Location 2	Location 3	Location 4	Corporate
Revenue		10,353,683.14	5,421,643.61	2,046,839.24	563,565.11	2,321,635.18	-
Non labor cost of sales		2,760,638.81	1,487,360.34	457,298.92	64,394.25	751,585.30	-
<b>Gross Profit</b>		7,593,044.33	3,934,283.28	1,589,540.31	499,170.86	1,570,049.88	-
	<i>as % to Sales</i>	73.34%	72.57%	77.66%	88.57%	67.63%	
Direct Labor		3,506,405.74	1,914,299.93	629,067.51	188,096.10	774,942.19	-
<b>Contribution Margin (CM)</b>		4,086,638.60	2,019,983.35	960,472.80	311,074.76	795,107.69	-
	<i>as % to Sales</i>	39.47%	37.26%	46.92%	55.20%	34.25%	
	<i>Direct LER</i>	2.17	2.06	2.53	2.65	2.03	
<b>Corporate Expenses:</b>							
Management Labor		1,369,976.41	435,352.00	260,978.00	90,012.00	155,789.00	427,845.41
Payroll taxes & benefits		1,047,581.08	414,040.96	234,194.81	77,191.73	240,762.41	81,391.18
Other operating expenses		865,267.08	342,383.78	147,346.10	33,952.29	142,323.60	199,261.31
<b>Total Operating Expenses</b>		3,282,824.57	1,191,776.74	642,518.90	201,156.02	538,875.01	708,497.89
	<i>as % to Sales</i>	31.71%	21.98%	31.39%	35.69%	23.21%	
	<i>Management LER to CM</i>	2.98	4.64	3.68	3.46	5.10	
<b>Net Operating Income</b>		803,814.03	828,206.61	317,953.90	109,918.74	256,232.68	(708,497.89)
	<i>as % to Sales</i>	7.76%	15.28%	15.53%	19.50%	11.04%	
	<i>as % to GP</i>	10.59%	21.05%	20.00%	22.02%	16.32%	
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Depreciation		(320,237.01)	(215,058.31)	(17,158.71)	(20,477.47)	(57,090.62)	(10,451.89)
Other income		892.51	-	-	-	-	892.51
<b>Total Other Income (Expense)</b>		(459,199.16)	(289,655.94)	(20,526.34)	(40,646.52)	(68,548.91)	(39,821.46)
<b>Net Income</b>		344,614.87	538,550.67	297,427.56	69,272.22	187,683.77	(748,319.35)
	<i>as % to Sales</i>	3.33%	9.93%	14.53%	12.29%	8.08%	
Corporate LER (All CM per Corp Labor)		9.55					

**Company-Wide Picture by Year**

Better
Worse

	2011	2012
Revenue	9,965,998.98	10,353,683.14
Non labor cost of sales	2,622,606.87	2,760,638.81
<b>Gross Profit</b>	7,343,392.12	7,593,044.33
<i>as % to Sales</i>	73.68%	73.34%
Direct Labor	3,083,085.45	
<b>Contribution Margin (CM)</b>	4,260,306.67	
<i>as % to Sales</i>	42.75%	
<i>Direct LER</i>	2.38	
<b>Corporate Expenses:</b>		
Management Labor	1,301,477.59	
Payroll taxes & benefits	995,202.03	
Other operating expenses	813,003.72	
<b>Total Operating Expenses</b>	3,109,683.34	
<i>as % to Sales</i>	31.20%	
<i>Management LER to CM</i>	3.27	
<b>Net Operating Income</b>	1,150,623.33	
<i>as % to Sales</i>	11.55%	
<i>as % to GP</i>	15.67%	
<b>Other Income (Expense):</b>		
Interest expense	(132,861.93)	
Depreciation	(304,225.16)	
Other income	847.88	
<b>Total Other Income (Expense)</b>	(436,239.20)	
<b>Net Income</b>	714,384.13	
<i>as % to Sales</i>	7.17%	

Let's grow!

PR Taxes as a % of all labor	22.70%
Corporate Labor	406,453.14
Corp LER (corp CM per Corp Labor\$)	10.48

**Company-Wide Picture by Year**

Better  
Worse

	2011	2012
Revenue	9,965,998.98	10,353,683.14
Non labor cost of sales	2,622,606.87	2,760,638.81
<b>Gross Profit</b>	7,343,392.12	7,593,044.33
<i>as % to Sales</i>	73.68%	73.34%
Direct Labor	3,083,085.45	3,506,405.74
<b>Contribution Margin (CM)</b>	4,260,306.67	
<i>as % to Sales</i>	42.75%	
<i>Direct LER</i>	2.38	
<b>Corporate Expenses:</b>		
Management Labor	1,301,477.59	1,369,976.41
Payroll taxes & benefits	995,202.03	
Other operating expenses	813,003.72	
<b>Total Operating Expenses</b>	3,109,683.34	
<i>as % to Sales</i>	31.20%	
<i>Management LER to CM</i>	3.27	
<b>Net Operating Income</b>	1,150,623.33	
<i>as % to Sales</i>	11.55%	
<i>as % to GP</i>	15.67%	
<b>Other Income (Expense):</b>		
Interest expense	(132,861.93)	
Depreciation	(304,225.16)	
Other income	847.88	
<b>Total Other Income (Expense)</b>	(436,239.20)	
<b>Net Income</b>	714,384.13	
<i>as % to Sales</i>	7.17%	

If we grow, we have to add labor, right?

PR Taxes as a % of all labor	22.70%
Corporate Labor	406,453.14
Corp LER (corp CM per Corp Labor\$)	10.48

**Company-Wide Picture by Year**

Better  
Worse

	2011	2012
Revenue	9,965,998.98	10,353,683.14
Non labor cost of sales	2,622,606.87	2,760,638.81
<b>Gross Profit</b>	7,343,392.12	7,593,044.33
<i>as % to Sales</i>	73.68%	73.34%
Direct Labor	3,083,085.45	3,506,405.74
<b>Contribution Margin (CM)</b>	4,260,306.67	4,086,638.60
<i>as % to Sales</i>	42.75%	39.47%
<i>Direct LER</i>	2.38	2.17
<b>Corporate Expenses:</b>		
Management Labor	1,301,477.59	1,369,976.41
Payroll taxes & benefits	995,202.03	1,047,581.08
Other operating expenses	813,003.72	865,267.08
<b>Total Operating Expenses</b>	3,109,683.34	3,282,824.57
<i>as % to Sales</i>	31.20%	31.71%
<i>Management LER to CM</i>	3.27	2.98
<b>Net Operating Income</b>	1,150,623.33	803,814.03
<i>as % to Sales</i>	11.55%	7.76%
<i>as % to GP</i>	15.67%	10.59%
<b>Other Income (Expense):</b>		
Interest expense	(132,861.93)	(139,854.66)
Depreciation	(304,225.16)	(320,237.01)
Other income	847.88	892.51
<b>Total Other Income (Expense)</b>	(436,239.20)	(459,199.16)
<b>Net Income</b>	714,384.13	344,614.87
<i>as % to Sales</i>	7.17%	3.33%
PR Taxes as a % of all labor	22.70%	21.48%
Corporate Labor	406,453.14	427,845.41
Corp LER (corp CM per Corp Labor\$)	10.48	9.55

Classic example of growth with no profit!

**Company-Wide Picture by Year**

				Hold Constant	
				Growth Required	
				Options	
		2011	2012	Grow	Cut
Revenue		9,965,998.98	10,353,683.14	11,326,337.75	10,179,153.09
Non labor cost of sales		2,622,606.87	2,760,638.81	2,981,092.09	2,679,153.09
<b>Gross Profit</b>		7,343,392.12	7,593,044.33	8,345,245.65	7,500,000.00
	<i>as % to Sales</i>	73.68%	73.34%	73.68%	73.68%
Direct Labor		3,083,085.45	3,506,405.74	3,506,405.74	3,000,000.00
<b>Contribution Margin (CM)</b>		4,260,306.67	4,086,638.60	4,479,822.85	4,251,000.00
	<i>as % to Sales</i>	42.75%	39.47%	39.55%	41.76%
	<i>Direct LER</i>	2.38	2.17	2.38	2.50
<b>Corporate Expenses:</b>					
Management Labor		1,301,477.59	1,369,976.41	1,369,976.41	1,300,000.00
Payroll taxes & benefits		995,202.03	1,047,581.08	1,047,446.88	923,640.00
Other operating expenses		813,003.72	865,267.08	865,267.08	865,267.08
<b>Total Operating Expenses</b>		3,109,683.34	3,282,824.57	3,282,690.37	3,088,907.08
	<i>as % to Sales</i>	31.20%	31.71%	28.98%	30.35%
	<i>Management LER to CM</i>	3.27	2.98	3.27	3.27
<b>Net Operating Income</b>		1,150,623.33	803,814.03	1,197,132.48	1,162,092.92
	<i>as % to Sales</i>	11.55%	7.76%	10.57%	11.42%
	<i>as % to GP</i>	15.67%	10.59%	14.35%	15.49%
<b>Other Income (Expense):</b>					
Interest expense		(132,861.93)	(139,854.66)	(139,854.66)	(139,854.66)
Depreciation		(304,225.16)	(320,237.01)	(320,237.01)	(320,237.01)
Other income		847.88	892.51	892.51	892.51
<b>Total Other Income (Expense)</b>		(436,239.20)	(459,199.16)	(459,199.16)	(459,199.16)
<b>Net Income</b>		714,384.13	344,614.87	737,933.32	702,893.76
	<i>as % to Sales</i>	7.17%	3.33%	6.52%	6.91%
PR Taxes as a % of all labor		22.70%	21.48%	21.48%	21.48%
Corporate Labor		406,453.14	427,845.41	427,845.41	357,869.00
Corp LER (corp CM per Corp Labor\$)		10.48	9.55	10.47	11.88



**Company-Wide Picture by Year**

				Cut	
				Increase	
				Options	
		2011	2012	Grow	Cut
Revenue		9,965,998.98	10,353,683.14	11,326,337.75	10,179,153.09
Non labor cost of sales		2,622,606.87	2,760,638.81	2,981,092.09	2,679,153.09
<b>Gross Profit</b>		7,343,392.12	7,593,044.33	8,345,245.65	7,500,000.00
	<i>as % to Sales</i>	73.68%	73.34%	73.68%	73.68%
Direct Labor		3,083,085.45	3,506,405.74	3,506,405.74	3,000,000.00
<b>Contribution Margin (CM)</b>		4,260,306.67	4,086,638.60	4,479,822.85	4,251,000.00
	<i>as % to Sales</i>	42.75%	39.47%	39.55%	41.76%
	<i>Direct LER</i>	2.38	2.17	2.38	2.50
<b>Corporate Expenses:</b>					
Management Labor		1,301,477.59	1,369,976.41	1,369,976.41	1,300,000.00
Payroll taxes & benefits		995,202.03	1,047,581.08	1,047,446.88	923,640.00
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<b>Other Income (Expense):</b>					
Interest expense		(132,861.93)	(139,854.66)	(139,854.66)	(139,854.66)
Depreciation		(304,225.16)	(320,237.01)	(320,237.01)	(320,237.01)
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Corp LER (corp CM per Corp Labor\$)		10.48	9.55	10.47	11.88

# Labor Efficiency Ratio by Employee

- Service business example
  - Able to track revenue generated by person
  - More precise than typical Utilization Rate method
  - Dynamic of productivity between full-time staff and part-time staff
  - How to determine target performance



LER by Employee

Employee	Revenue	Labor Cost	LER	Contribution Margin	CM Rank
FT Emp 1	162,799.19	44,437.91 \$	3.66	118,361.28	3
FT Emp 2	133,953.67	38,588.30 \$	3.47	95,365.37	4
FT Emp 3 (Less than 1 year)	47,516.97	13,849.28 \$	3.43	33,667.69	14
FT Emp 4 (Less than 1 year)	64,973.73	20,370.65 \$	3.19	44,603.08	11
FT Emp 5	234,034.69	76,984.49 \$	3.04	157,050.20	1
FT Emp 6 (Less than 1 year)	32,396.81	10,783.46 \$	3.00	21,613.35	17
FT Emp 7	209,126.69	71,026.71 \$	2.94	138,099.98	2
FT Emp 8	107,565.30	38,937.72 \$	2.76	68,627.58	6
PT Emp 1	124,621.11	45,518.45 \$	2.74	79,102.66	5
PT Emp 2	106,448.53	39,524.59 \$	2.69	66,923.94	7
PT Emp 3	110,586.12	45,714.41 \$	2.42	64,871.71	8
PT Emp 4	103,976.10	48,436.28 \$	2.15	55,539.82	9
PT Emp 5	65,362.72	37,403.99 \$	1.75	27,958.73	16
PT Emp 6	88,704.35	60,627.90 \$	1.46	28,076.45	15
Owner 1	157,598.42	110,422.47 \$	1.43	47,175.95	10
Owner 2	154,531.61	110,662.48 \$	1.40	43,869.13	12
Owner 3	168,266.38	127,570.34 \$	1.32	40,696.04	13
Total	2,072,462.39	940,859.43 \$	2.20	1,131,602.96	

LER by Employee

Below Avg

Employee	Revenue	Labor Cost	LER	Contribution Margin	CM Rank
FT Emp 1	162,799.19	44,437.91 \$	3.66	118,361.28	3
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LER by Employee

Target

Employee	Revenue	Labor Cost	LER	Contribution Margin	CM Rank
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**Be careful with Part-time staff!**

# 4 Critical Number\$

- Contribution Margin \$
- Direct LER
- Management LER
- Core Capital Target



# Strategy Process

- List Dangers impacting your business
- List Opportunities
- List Strengths





# Strategy Process - Continued

- Clear Dangers by having an Opportunity or Strength to clear the Danger.
- If you do not have one listed, “Create an Opportunity” (as Jack Welch said “Look for the train wreck and that is where the opportunity is”)



# Strategy Process - Continued

- Filter Opportunities down to the 5 most critical
  - (many will be saying the same thing in a different way or will be an action of a larger priority)
- Once you have your Top 5, do the Hoshin priority process



# Strategy Process – Hoshin example

Integration of Management Team

Maintain profitability targets

Staff Training

Document systems and processes

Skilled Labor development Plan



# Strategy Process – Hoshin example

Integration of Management Team

Maintain profitability targets

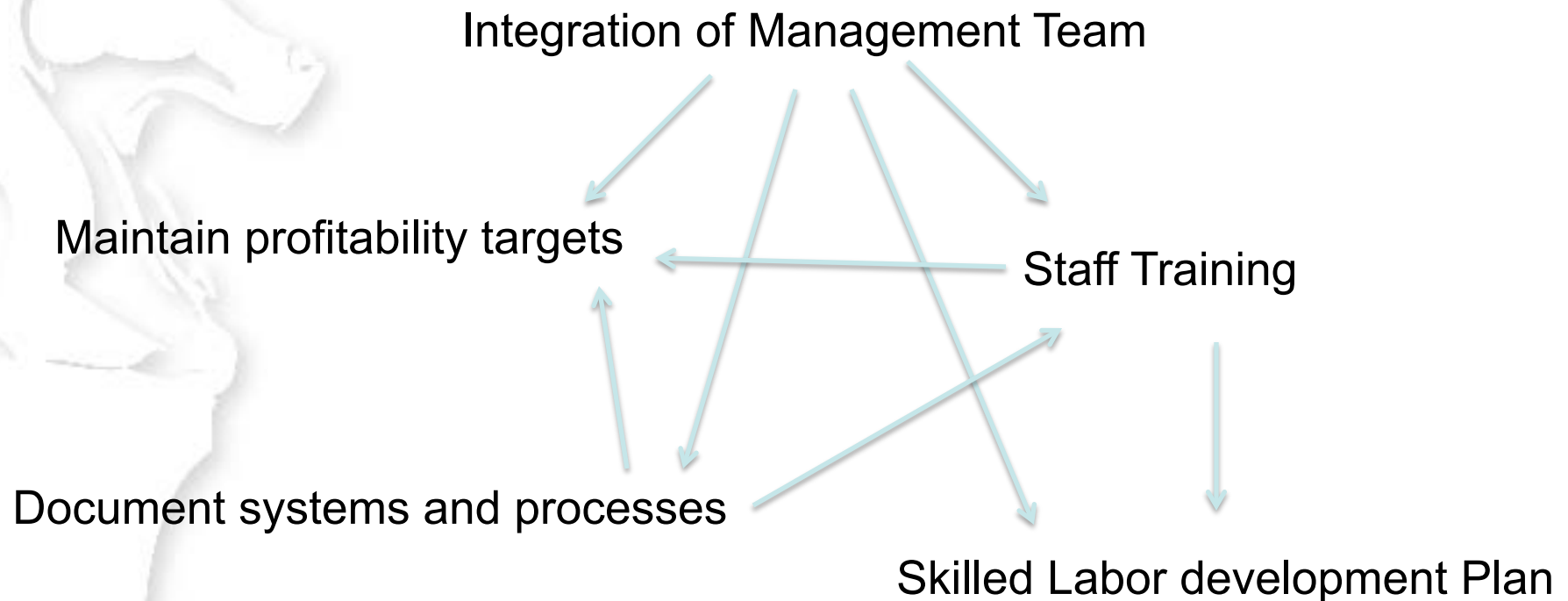
Staff Training

Document systems and processes

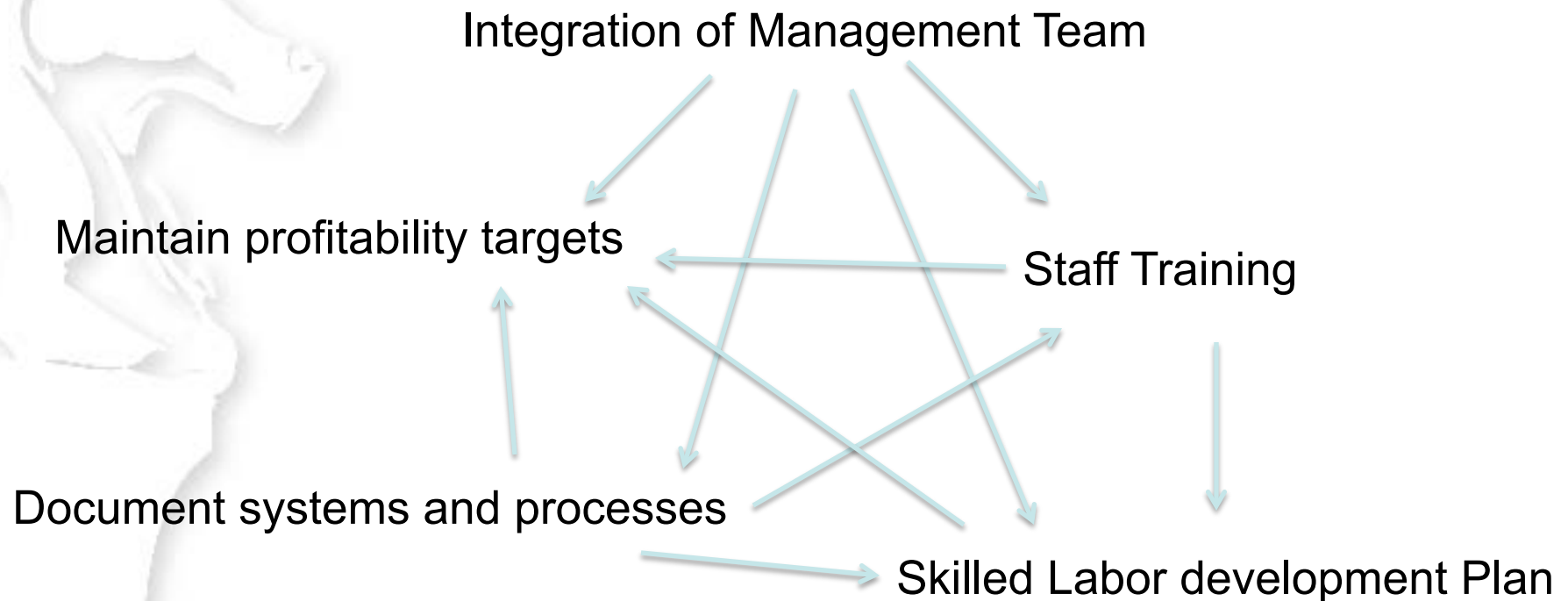
Skilled Labor development Plan



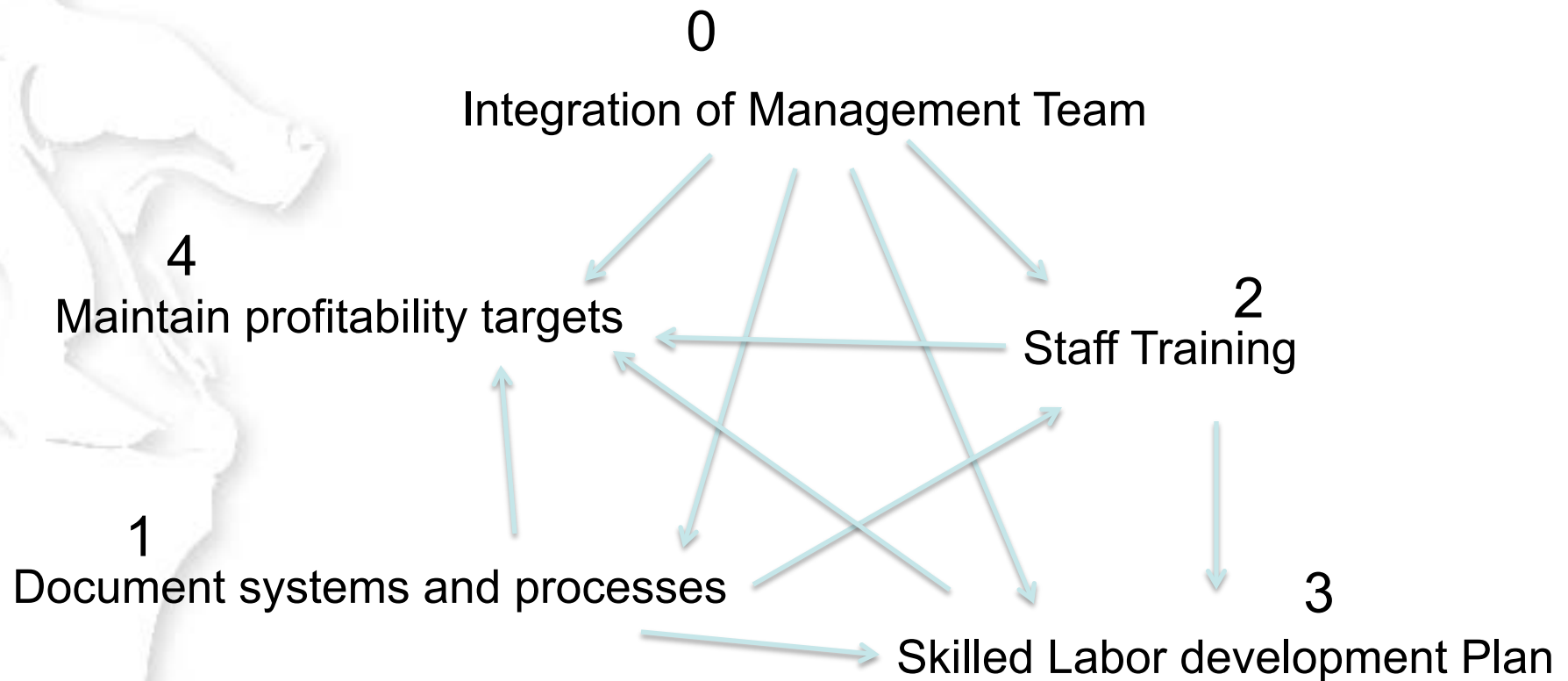
# Strategy Process – Hoshin example



# Strategy Process – Hoshin example



# Strategy Process – Hoshin example



# Strategy Process – Hoshin example

## Recap

1. Integration of Management Team
2. Documentation of Systems and Process
3. Staff Training
4. Skilled Labor Development Plan
5. Maintain Profit Targets





# Recap

- Define the side of the cube you have the data to track
- If you do not have it historically, commit to start tracking
- Find the best, the worst and the average
- Get the bottom up to middle
- Then.....



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FOREWORD BY VERNE HARNISH, CEO, GAZELLES, INC.  
AUTHOR, MASTERING THE ROCKEFELLER HABITS

**SIMPLE  
NUMBERS,  
STRAIGHT TALK,  
BIG PROFITS!**

4 KEYS TO UNLOCK YOUR  
BUSINESS POTENTIAL

**GREG CRABTREE**

WITH BEVERLY BLAIR HARZOG