

Practice Kicking Yourself With Your Jerking Knee to Earn More Profit

New circumstances are most often first perceived as a threat when budgeted profit or cash flow objectives are not met. Since such potential shortfalls are happening somewhere almost all the time in enterprises, the organization's first reaction is to look for relatively painless ways to cut costs to overcome the shortfall. This tendency is reinforced by the likelihood that all the senior people in the company receive much of their annual bonus for meeting budgeted results. This so-called "incentive" creates a common interest in smoothing over the bump in the road so the company can grow profit and cash flow results at the rate it had planned. Enterprises that have public shareholders receive a double incentive to meet this goal because additional compensation is tied up in stock options that will fall in value if shareholders are disappointed in company results. Finally, if the shortfall cannot be overcome, heads will roll in some cases. That threat is never far from many peoples' minds in an organization. For most companies, this standard operating procedure often turns into a mad scramble to cut costs that permits little room or time for thought about the long-term consequences. For example, for about two decades a well-known packaged goods company had an earnings shortfall early in almost every year in its largest division. The first planned expense to be cut in each case was the money for promotions designed to create more brand loyalty among consumers. Year after year, loyalty to the company's brands in that division dropped, and profits slumped. But company executives often restored enough profit performance to save some part of their bonus. How? They used defensive strategies. For instance, they offered special incentives to retailers to purchase products at the end of every year so that retailers often bought four to six months' supply at one time. This meant that the products were often less than perfect when used, and all consumers were trained to look for annual "give-away" price reductions that discouraged them from buying the products year round at full price. Brand loyalty was further harmed as a result. For this company, reactions to the hostile environment characterized by a decrease of loyal consumers were made worse by the actions taken to protect the budgets. The real solutions (finally taken about twenty years after the irresistible force problem arose) were to improve the quality of the products and to build brand loyalty among the consumers. To facilitate these solutions, the annual "year-end load" was eliminated.

About the Author

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