Take
Action
Series

Managing Growth

The Silent Killer

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the business knowledge center
Go-To Solutions for Small Business

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Overview

The objective of this manual is to alert you to the phenomena called, “growth”. It will outline what happens to a business that grows beyond its sustainable growth rate—uncontrolled growth kills. In addition to discussing the three different scenarios for growth, we will discuss the underlying assumptions associated with your company's sustainable growth rate. Finally we will explore business strategies that enable you to break the handcuffs established by adhering to sustainable growth and enable your business to reach for the stars.

GROW! That’s the marching order of every business owner. An order that’s easy to follow because it is only rational to believe the more your business sells the more it makes, and the more it makes, the happier you will be. That sounds very logical to us. If only it was that easy. We are going to assume as a business owner/manager you also believe in growth because it is the American Way. American business owners firmly believe bigger is better, those with the most toys win, and in business, growth is equated to success.

Our goal is to provide you with a basic understanding of the financial ramifications of growth. This publication does not address the psychological or physical issues that must also be addressed when you are in the growth mode.

Business Truths

Before we begin our discussion on growth, let me state right up front, we believe your business has to constantly grow or it will die. we are advocates for growth; growth that is controlled. In order to appreciate our discussion there are some fundamental business facts/truths that every business owner must buy into. They are:

1. ASSETS = LIABILITIES + EQUITY
This equation lays the foundation for doing business. It represents the structure of the balance sheet which serves as the foundation of any business. It states what a business owns (Assets) must equal the sources of funding (Liabilities which is debt funding and Equity which is ownership funding). The left-hand side of the balance sheet represents the tools owned by a business to generate sales; while the right-hand side represents how the business pays for those tools. They must always be in balance with one another.

2. SALES REQUIRE ASSETS.
Businesses typically generate revenue by selling assets (inventory) which differs by industry sectors. They also need to have other assets like cash and accounts receivable to support sales. At the end of the day all businesses should be in the same business, the business of making money. What makes your business different is the asset base you need to generate/support your company's sales production.

Sustainable Growth Rate Worksheet — [Maintain D/E Ratio]

Gather information from your latest year-end balance sheet and income statement then follow these steps:

STEP 1. FROM BALANCE SHEET

$$\frac{\text{Record Total Liabilities}}{\text{Record Equity}} = \frac{\qquad\qquad}{\qquad\qquad} = \underline{\qquad\qquad} \ \text{D/E}$$

[Debt to Equity]

STEP 2. FROM BALANCE SHEET & INCOME STATEMENT

$$\frac{\text{Record Total Assets}}{\text{Record Total Sales}} = \frac{\qquad\qquad}{\qquad\qquad} = \underline{\qquad\qquad}\ \% \quad \text{VA\%}$$

[Variable Asset %]

STEP 3. FROM INCOME STATEMENT

$$\frac{\text{Record Net Income*}}{\text{Record Total Sales}} = \frac{\qquad\qquad}{\qquad\qquad} = \underline{\qquad\qquad}\ \% \quad \text{NP\%}$$

[Net Profit %]

STEP 4. USING COMPUTED DATA

Record data into formula and calculate. Remember to express % as real number, i.e. move decimal point two places to the left.

$$\frac{\text{Net Profit \% x (1 + D/E)}}{\text{Variable Asset \% – [Net Profit \% x (1 + D/E)]}} = \underline{\qquad\qquad} = \underline{\qquad\qquad}\ \%$$

Annual Sales Growth Rate

Note: If you maintain your historical financial performance this annual sales growth is what your business can afford in the next twelve months and not witness a deterioration of your D/E ratio.

Printed in the United States of America