



Looking for a Profit in 2009

Stuart W. Margolis, CPA. MT

Published in GAA UpDate 2009

Everyone is looking for creative ways to stay in the black for 2009. Answers might be found in your own management tactics. Surprisingly, the use of value-added in estimating, costing and pricing is still foreign to many printing managers. However, understanding value-added enables managers to gain a better understanding of the behavior of costs and apply a manufacturing strategy that leads to a competitive advantage and helps maximize profits.

Each year, significant dollars disguised as unrealized potential profits go out the door. Take the printing manager who sends work out, even though he could do the job in-house. What he's really doing is sending profits down the street.

Example:

A sign and digital printer supported each of its three principals on comfortable salaries. The company's operating report was always the same: \$750,000 in

quarterly sales, and a pre-tax profit of \$75,000. Suddenly, profits dipped to \$25,000 in a single quarter.

In reviewing the report, outside service costs were high. Management justified it by saying when an internal estimate on a sign job is too high, they bid the job out to two sign printers in another part of the country. "The other firms can do the job cheaper which allows the company to sell the job at a lower price and consequently, log a profit on the cost sheet," they said.

What they actually had done, however, was pay for the job twice. They understood they had paid the outside sign printer. What they didn't realize was that they already paid for the job in the cost of their operation -- payroll, factory, administration, selling, and other costs. Since they could have done the job without any incremental cost, the outside purchase was an unnecessary expense.

(Continued)

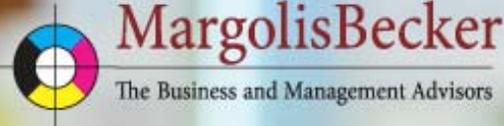
“Understanding value-added enables managers to gain a better understanding of the behavior of costs...that... helps maximize profits.”

Washington, DC Philadelphia

10001 Derekwood Lane, Suite 210 555 City Line Avenue, Suite 460

Lanham, MD 20706 Bala Cynwyd, PA 19004

888.577.1717 p 301.577.1313 f 301.577.0431 888.577.1717 p 610.667.4310 f 610.667.2099



Looking for a Profit in 2009

Stuart W. Margolis, CPA, MT *(Continued)*

This is not uncommon, but it illustrates the danger of unnecessarily sending services out. This practice is commonly referred to as "loss of profit."

Sometimes, of course, a job must be sent out. A company can't produce a wide format banner if it doesn't have the equipment to do it. It can't produce a job if it is operating at full capacity. Nor can it produce two jobs on one press at the exact same time (yet).

Except for unavoidable circumstances like these examples, however, it's always advantageous to keep jobs inside. The really successful companies figure out

ways to make "unavoidable circumstances" avoidable!

The "formula for success" is noted below.

Why is this concept still an unsolved mystery to some? Because companies can have a significant sales increase while seeing value-added and profits fall. If a management team is focused solely on sales, they can miss significant factors.

We all understand that there can be many reasons for poor operating performance. However, in the hundreds of printing companies we've consulted, we have found that

in many cases, poor performance stems from failure to stick to this financial premise.

Profits are made from the sales of products or services that a company "manufactures."

Find your niche. Find your sweet spot. Communicate it to your sales team.

The value-added concept is a practical and easy way to look at the effect of marginal contribution. A basic "rule" to remember is: "Value-added," or "Sales less materials and outside services," contributes to cover overhead.

(Continued)

The formula for success is:

1.) Sales	X	
Less:		
Materials	<u>X</u>	
	X	*
Value-Added		

2.) Less: Overhead X *(which remains relatively fixed within a range)*

3.) Produces Profit X

** Therefore, the theme is to maximize value-added.*





MargolisBecker
The Business and Management Advisors

Looking for a Profit in 2009

Stuart W. Margolis, CPA, MT *(Continued)*

In an industry where fixed costs predominate the local printer, it is important to successfully do everything in-house that you can. Why? Because fixed costs remain the same whether work goes out or stays in. A sound policy would be: **We do all work inside unless we *must* send it out.**

To understand the behavior of costs, let's take a look at the following example (simplified to demonstrate the effect of variable costs on contributions):

A printing company had sales that went from \$800,000 in the first year to \$1 million in the second year (an increase of 20%). The value-added increased by the same percentage of 20%, or \$134,000. The variable-overhead cost also increased by the same ratio as sales and value-added, with fixed costs remaining the same as the previous year.

A marginal contribution of \$92,800 was realized. The entire marginal contribution went to the bottom line.

	<u>2008</u>	<u>2007</u>
Sales	\$1,000,000	\$800,000
Materials	<u>330,000</u>	<u>264,000</u>
Value Added	670,000	536,000
Less: Variable Overhead Expenses	<u>206,000</u>	<u>164,800</u>
Marginal Contribution	464,000	371,200
Less: Fixed Overhead Expenses	<u>364,000</u>	<u>364,000</u>
Income Before Taxes	<u>\$ 100,000</u>	<u>\$ 7,200</u>

Any increase in value-added contributes to cover fixed overhead costs and then increases profits.

Fortunately, there's nothing mysterious or even difficult about using value-added management to turn around situations. Value-added is a simple, valid and critical concept. It has helped some of the most successful printing companies extract more and more profits from their sales.

Want to see what margins other printers are achieving? I don't blame you. I would too. Look no further than the Annual PIA Ratios. The annual survey is hot off the press and will be available until April 2009. Printers can download the form, fill it out and get a copy of a resulting report for free. *(Continued)*

“A sound policy would be:

We do all work inside unless we must send it out.”



Looking for a Profit in 2009

Stuart W. Margolis, CPA, MT *(Continued)*

To participate in the survey, go to:

www.margolisbecker.com/ratio.

If you've never filled out the annual PIA Ratio Survey before, do it this year. During times of drastic economic swings and fluctuations, it is critical to understand *your* industry and *your* competitors. Make it a priority to fill the survey out and get a free copy of the results for the next five years. Knowledge is power. Keep the edge.

To learn more call me and request a book on the Value-added concept.

The PIA Ratio Survey is available at:

www.margolisbecker.com/ratio

Fill it out for your free report copy!

MargolisBecker, The Business and Management Advisors, is a CPA firm specializing in the graphic arts industry.

Whatever your goals and needs, we have the solution. Our services include strategic planning, business valuations, mergers & acquisitions, turnaround management, accounting, auditing and tax compliance. The Company has prepared the PIA/GATF Ratio Studies since 1960.

If you have any comments or questions, you may reach us at:

888-577-1717

or

talk.to.us@margolisbecker.com



*Stuart W. Margolis
CPA, MT*