Modern Brewery Age
The Business Magazine for the Beer Industry

The "Red Flags" of Declining Value

By Lamont Seckman

Managing your company with an eye toward value is always a good idea - ***especially during a period of industry consolidation***. If your company is a potential sell candidate, value maximization has obvious benefits. For potential buyers, increased business value provides additional cash flow and borrowing power to finance acquisitions.

Our experience working with wholesalers on value enhancement strategies indicates common trends in operations that have lost value. These trends are "red flags" that can warn of impending value declines long before the year-end profit-and-loss statements come back from the accountants.

No Clear Strategy

One of the most common weaknesses in companies experiencing value erosion is the ***lack of a clearly defined strategy*** and supporting performance objectives that is communicated to and understood by the entire organization. This situation makes managers and key employees feel that they receive little or no direction from the top. Companies without direction from the top are usually inefficient, unfocused and have a workforce lacking in motivation. Companies in this situation are effectively operating on "autopilot." **Do not be fooled!** Such a situation can continue for a period of time without obvious repercussions, especially if you have good people working for you. However, even the best-intentioned employees will eventually become too comfortable or too frustrated with this work environment and will respond by ratcheting their performance levels down.

The "Entitlement" Mentality

Many underperforming wholesalers have created a work environment in which employees feel entitled to the continuing benefits of a successful operation - even while corporate profits are trending down. This can be caused by poorly designed compensation systems that do not adequately link pay to performance. In addition, many wholesalers do not disclose operating or even gross margin information to employees, which can lead to a misunderstanding of the severity of performance declines. As companies become larger and more complex, the strategy of limited information dissemination should be rethought. Managers are operating in a void if not provided with good, timely, and relevant performance information. We find poor information reporting to be endemic to this industry. Many information systems simply do not provide useful, summary performance data to aid in executive management decision making. Do not let this be an excuse. A common red flag in companies losing value is when key managers cannot answer such fundamental questions as: "*How much does it cost to deliver a case of beer*?" or "*How have productivity levels trended in the warehouse*?"

The first step in addressing this red flag is knowing what information needs to be gathered to allow managers to make informed decisions. Do not let your computer system be the limiting factor. **Find a way to get the information and report it in a useful fashion!**

Poor Training and Development

Many managers are ignorant of the information needed to improve operations. In most cases, this is due to inadequate training and development. Good managers are in short supply in the beer distribution industry, and poor training is one reason. Limiting your managerial training to brewery-sponsored seminars where early afternoon tee-times punctuate the days' learning will not cut it in the new business environment.

Inventory Control Problems

Interestingly enough, a significant trend among value losers relates to inventory control. It is easy to blame shrinking margins on increased discounting and brewery initiatives on out-of-code product. In reality, an increasing cost-of-goods as a percentage of sales can indicate the presence of a variety of operational problems including poor quality load-out procedures resulting in increased breakage, loose controls on the sales staff resulting in greater aged product write-offs, and declining morale among the employees resulting in theft and increased on-truck and warehouse breakage.

Summary

Remember, high-volume growth and strong gross margin percentages can hide many operating inefficiencies. As growth opportunities dwindle and downward pressures on margins increase, owners should pay more attention to the "red flags" that may portend a decline in value. Addressing these flags early in a positive way may prevent some rude surprises in the company's profit-and-loss statements.

"Red Flag" Indicators:

Answering "**No**" to the following questions *may* indicate the presence of "Red Flags":

- ✓ Do your key managers/employees have a ***true*** understanding of the company's strategy?
- ✓ Do your employees have a positive work attitude?
- ✓ Are your employees really aware of the company's performance trends?
- ✓ Is your sales force hungry and/or motivated?
- ✓ Is compensation used effectively to incent *and direct* key managers and employees?
- ✓ Do your employees feel their pay is related to their performance?
- ✓ Can managers answer key questions on the costs of warehousing, selling, and delivering beer?
- ✓ Do your managers use non-financial measures to develop performance objectives and assess performance?