Diversify Your Business Income

For the past few columns I have focused on business income and one of the statements that I made was that a business owner should consider diversifying the company’s income. I will close this series by making a few comments and observations about this topic.

Handled properly, diversification can reduce financial risk and improve cash flow. For example when Toys R Us began selling diapers in order to attract customers during slow selling seasons, it was a great business decision. But an unsuccessful diversification can drain cash and divert a business from its mission.

What exactly does it mean to diversify? There are four common business models:

- **Sell a new related product or service.** Example: Celestial Seasonings, known for selling tea, began selling coffee.
- **Adopt existing products or technology.** Examples: The military Humvee was converted to the consumer Hummer; the makers of Arm & Hammer baking soda sold Arm & Hammer Baking Soda Tooth Powder.
- **Offer a new unrelated product or service.** Example: The Virgin retail chain went into the airline and mobile phone businesses.
- **Offer products or services that compete with your suppliers or customers.** Examples: Armani opened retail stores; Netflix began producing and distributing movies.

But consider this carefully. One of my SCORE mentor colleagues, Charles Pagenhart cautions "If you're going to seek a diversified source of revenue from different products, then these products should be central and complimentary to the business. The diversification needs to have logic.” A plumbing service might very well do heating. An auto dealership might stock pickups but they may or may not stock delivery vans. It really depends on what the business can handle. A concentration in one area can leave you vulnerable. At the same time diversification should not be the cause of a product glut. Simply having a proliferation of products is not the answer.

Diversification of revenue may also include advertising revenue. For example, many companies who have established an online presence have learned that additional revenue
can be generated by including Google ads, affiliate programs (where the company gets paid when someone buys another company's product or service) or the use of banner ads.

Not everyone is a fan of diversification. "It can get you in trouble by leading you away from your vision and goals and it can cause mounting costs," says SCORE mentor Gerald Dallmann." Find what you're good at and stay within that. If you're in the furniture business, don't start selling snow cones unless it will keep the kids occupied while you’re selling the parents some furniture."

Before you diversify, consider the following questions:

- Do you have a good reason for diversifying? You should have a reason. For example, seasonal sales that justifies taking time away from your primary products or services.
- Is the timing right? Are you diversifying at a time when you (and your management) need to remain focused on the core business?
- Do you have the skills and knowledge? Do you have what it takes to successfully promote a new service or product? Without the ability to promote a diversified line, you're headed for a dilemma.
- Have you considered the effects? The rewards from diversity should offset some weakness in your current business. For example, a diversified line should provide you with income during an otherwise slow period.
- Have you projected the potential for failure? If a worst-case scenario shows that diversification will sink your business, you may not want to take the risk.
- Is diversification a logical extension for your company? If you are a retailer, can you diversify by offering related services? For example if you sell knitting supplies, can you provide knitting lessons?

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