When Should a Small Business focus on Growth and Less on Profits?

A local small business CEO asked me an interesting question a couple of weeks ago. “Dean I have been in business now for almost 5 years. I love it. It is going quite well. But, I am getting a little bored so I am wondering when could I/should I start focusing on growth and less on profits?” Now, isn’t that a great question!

This made me start to really think about his business and also do some searching about the topic. In this search, I ran across a piece in a blog site called Quora that a friend of mine had written on this exact same topic….so I am going to give that to you. It comes from Tim Berry, who has for years done strategy consulting and who built Palo Alto Software without outside investment. I met with this CEO and gave him a copy of Tim’s response as we started to chat. Here is how Tim answered the question and I think it is a good one. He says…..

As soon as you have the cash flow managed, you should focus on growth, not profits.

Profits are today, and growth is tomorrow. You need today assured by cash flow, but don’t sacrifice more today than you have to when you pay for it with tomorrow. Find the right level.

Cash is what’s real; money in the bank. That’s much more important than profit. Growth, meaning higher sales, more customers, is also real. Within reasonable, limits, growth is more important than profit. Profit is an accounting and tax concept. You can be profitable and run out of money, and you can be unprofitable and have cash in the bank and grow.

Of course you need profits to survive. However, this question is more interesting than the quick answer implies. And notice the question is properly posed with the word “when,” which is the right way to put it. The real decision isn’t profits vs. growth (you choose profits in that binary world) but rather more profits vs. growth. This is one I lived with for a lot of years in a real business situation.

The underlying principal is hierarchy of values.

1. First, you have to cash flow assured (not that a small business ever really does, but let’s say reasonably assured).

2. Then you have to have some minimum level of profits (literally, in my business plan, and in management meetings, I specified 2% on sales as a comfortable upper limit on profits).

3. But after that – and here’s where this question gets interesting – you encounter a world of small decisions that pit growth against profits. You make choices on product quality, channels, and especially marketing that feel like money going either to build more growth or take home as profits.
I’ve had real-world experience with this for a lot of years and I’m really sure that my choice of priorities – I aimed for 2% profits on sales and 15%-50% growth in sales – worked very well for my business. We grew from a few hundred thousand dollars of sales to $5M annual sales in four years, without outside investors.

Of course the struggling small business that’s operating at the edge needs to focus on cash even more than profits. But a healthy small business, on the other hand, does have a choice between more profits and growth.

Ideally the question isn’t either profits or growth, but rather what’s the level of profits above which you shift those resources to growth. Think of it as a choice between today and tomorrow.

Thanks Tim! This gave us a great jumping off point in the coffee session with this CEO.

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Dean L. Swanson
Southeast Minnesota SCORE
c/o Rochester Area Chamber of Commerce
220 South Broadway, Suite 100
Rochester, MN 55904
www.seminnesota.score.org/
*Dean is a volunteer SCORE Mentor and Regional Vice President for the North West Region