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ABSTRACT

The first in a series of subject presentations in the field of administrative management for use by educators and businessmen who teach management courses is offered. The point is made that the concept of an educational program in small-business administrative management involves the investigation of a series of topics stemming from basic management functions as opposed to purely operational features of the business represented. The Lesson Plan is an outline of the material covered which may be used as a teaching guide, or as a framework for developing an individualized presentation. The Presentation is a carefully prepared subject presentation which may be used as written or modified to meet local needs and conditions. The Visual Aids are photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The Supply Department consists of materials which may be reproduced locally for distribution to course participants. Cases in Point list short actual small-business management cases which may be used to augment the presentation and to develop discussion. The Incubator provides ideas for stimulating further thought and discussion by the participants. A bibliography is provided, and field offices of the Small Business Administration are listed. (CK)

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SUCCESS and FAILURE FACTORS IN SMALL BUSINESS

ADMINISTRATIVE MANAGEMENT COURSE PROGRAM

Topic 1

SMALL BUSINESS ADMINISTRATION

1

ADMINISTRATIVE MANAGEMENT COURSE PROGRAM

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Small Business Administration

Washington, D. C. 20416 ● 1964

SMALL BUSINESS ADMINISTRATION

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FOREWORD

The Administrative Management Course Program was developed by the Small Business Administration in cooperation with educational institutions in 1954 to bring modern management knowledge and techniques to the owners and managers of small businesses. Since then, more than 700 American universities, colleges, and local school systems have cosponsored 2,500 courses with this Agency. Nearly 75,000 owners and managers of small businesses have attended these courses.

This is an outstanding demonstration of public spirit and service on the part of these hundreds of educational institutions. Yet, there remain many thousands of communities, particularly those under 25,000 in population and whose business establishments are all small, which have never had an administrative management course.

A committee on management education was recently formed consisting of representatives of the Distributive Education division of the American Vocational Association, and the Small Business Administration to study ways of meeting the small-business management needs of these small communities. The committee recommended that a series of subject presentations, including lesson plans, lectures, visual aids, case studies, and handout material, be developed to assist in the establishment of administrative management course programs in new locations. Further, it was felt that this material could materially assist existing management programs, particularly by emphasizing the importance of continuing education for small-business owners and managers, and by assisting the busy instructor with his preparation.

SBA accepted the responsibility for developing a series of subject presentations in the field of administrative management for use by educators and businessmen who teach these management courses. This booklet is the first in the series. We believe that these presentations will be particularly useful to Distributive Education in the smaller community where library research facilities are limited and equipment for the production of visual aids is not readily available.

I wish to express appreciation to the Richmond Public Schools System for granting a leave of absence to Mr. John O. Perreault. Mr. Perreault did the research and preliminary draft of the booklet under the supervision of Mr. Grant C. Moon, Chief, Management Courses and Conferences Division. Mr. George C. Willman, Jr. and Mr. John W. Clark, Educational Specialists in the Division, have edited and prepared the booklet for publication with the assistance of Misses Margaret Torpey and Cynthia Moreau. Artwork and visuals were prepared by Mr. Michael J. Fontana and Mr. Milton H. Weber of the Graphics Branch, Office of Administrative Services.

Eugene P. Foley
Administrator

May 1964

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A WORD ABOUT THIS SESSION

The concept of an educational program in small-business administrative management involves the investigation of a series of topics stemming from basic management functions as opposed to purely operational features of the business represented. The operational factors vary widely, but the principles of sound administrative management have quite universal application.

It is anticipated that, through the medium of administrative management courses or institutes, educational institutions will cooperate with the Small Business Administration and other community agencies in bringing the specialized knowledge and experience of a series of management specialists to small-business owners and managers participating in the program.

Typically, the "faculty" of a cosponsored management course might include:

A lawyer,
A banker or financial executive,
An advertising executive,
A Dun & Bradstreet, Inc. executive or a management consultant,
A trade association executive,
An accountant,
A Distributive Education coordinator,
A school or college faculty member, in specialized business administration or merchandising fields,
An SBA Management or Financial Specialist, and/or
Other businessmen.

This topic, Success and Failure Factors in Small Business, may be handled by a Dun & Bradstreet, Inc. executive or some other management specialist. The U. S. Office of Education publication, Guide for Part-Time Instructors, Distributive Education for Adults, may prove useful to local instructors.

This is one of a series of subject presentations which are available to the local educator. The complete set may be obtained from the Small Business Administration. Throughout the series, the term, "management," includes administrative, general, or top management.

The system of colored divider sheets is used in all booklets in the series. The color code is:

Grey -- The Lesson Plan. An outline of the material covered which may be used as a teaching guide, or as a framework for developing an individualized presentation. The lesson plan contains two columns: the left-hand column is an outline of the presentation; the right is a step-by-step indication of procedure, including chalk-board suggestions, quotations, discussion points, and a keyed guide to the visual aids supplied.

Rust -- The Presentation. A carefully prepared subject presentation which may be used as written or modified to meet local needs and conditions. It may also be used as a source of information by a person preparing his own lecture.

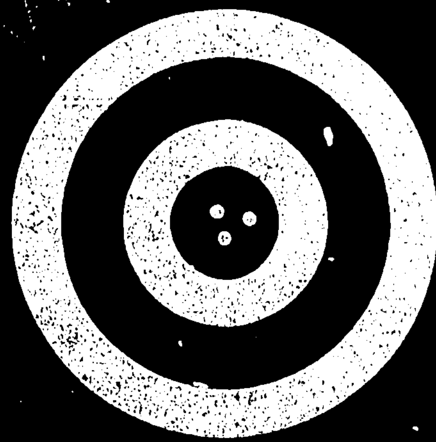
Buff -- The Visual Aids. Photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The subject presentation and lesson plan are keyed to the visuals. A set of visuals for each subject in this series may be borrowed from the nearest SBA regional office.

Green -- The Supply Department. Materials which may be reproduced locally for distribution to course participants. Your nearest SBA office can furnish information on current availability of SBA free publications, including titles published subsequent to this volume.

Yellow -- Cases in Point. Short actual small-business management cases which may be used to augment the presentation and to develop discussion, or as the basis for a second session on the same topic.

Blue -- The Incubator. Ideas for stimulating further thought and discussion by the participants. This material may be reproduced locally for distribution to course participants. "Assignments" are designed to aid in retention of the subject matter of the session.

NOTE: See back cover for index reference to the divider sheets.



STIMULATE GROUP BY SERVING AN INSTRUCTIONAL COCKTAIL

RECIPE

Use The Three B's (Bubbles)

- O ***Base*** instruction on problems at learners level.
- O ***Blend*** instruction with job experience.
- O ***Brighten*** instructions with variety of ***illustrations, investigations*** and group ***participation.***

FOUR BASIC STEPS OF INSTRUCTION

Instructing is like selling --

Selling

1. Approach customer
   - Promptness
   - Put at ease
   - Awaken ***interest***
2. Present merchandise or service
   - Select merchandise to fit need
   - Show one item at a time
   - Demonstrate ***selling points***
3. Have customer take part
   - Get merchandise into customer's hands
   - Let customer "try on" merchandise
   - Answer questions and meet objections
4. Bring sale to close
   - Help customers decide; ask: "which" "for whom" "when"
   - Be sure merchandise fits need
   - Summarize points of care and use
   - Handle mechanics of sale
   - Pave way for return visit

Instructing

1. Prepare the group
   - Start on schedule
   - Put group at ease
   - ***Awaken*** interest
2. Present information
   - Gauge material to needs
   - Present one point at a time
   - ***Show, illustrate, question***
3. Have group participate
   - Get group to ***discuss***
   - Have members ***demonstrate*** or ***use*** ideas
   - Answer questions and correct errors
4. Bring meeting to a close
   - Check on understanding; ask: "why" "how" "when" "what" "where" "who"
   - Be sure group now can use information
   - Summarize "take away" ideas
   - Make a definite conclusion
   - Pave way for next session

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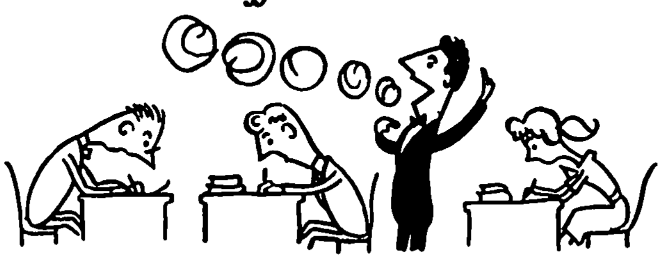
How To Deal With "Difficult Customers"



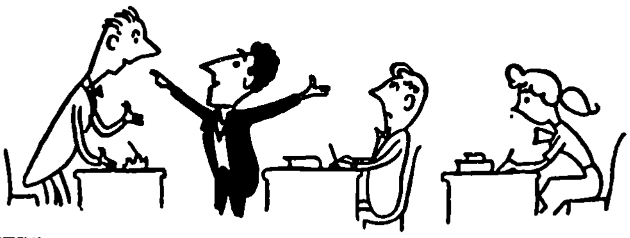
What To Do

THE "MOUTH"—wants to do all the talking.

Take the play away from him by asking others to comment on his remarks.

Deliberately turn to others and ask for their opinions. Avoid looking at him.

Tactfully ask him to give someone else a chance, or talk to him in private.

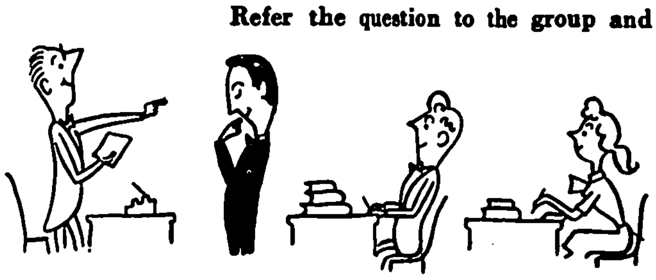


THE "ARGUER"—constantly tries to catch you up.

Keep cool. You can never "win" an argument. Always make him back it up. Ask for evidence.

Avoid getting personal.

Refer the question to the group and then to him.



THE "MOUSE"—is in every group.

Call him by name and ask him for an opinion. Ask him an easy question he is sure to answer well, then praise him. This person is worthy of your attention.

THE "SO-WHATER"—is disinterested.

Point up something he has done as a good example of the point being stressed. Ask direct questions affecting his work.

LESSON PLAN

TOPIC: SUCCESS AND FAILURE FACTORS IN SMALL BUSINESS

OBJECTIVES: To create an awareness as to the nature and sources of the real problems of small business.
To outline the common pitfalls and how they may be avoided.
To introduce the need for systematized "administrative management" as opposed to mere operations.

SESSION CONTENT	TIPS AND APPROACHES
I. MANAGEMENT IS EASIER WHEN YOU KNOW WHAT YOU'RE DOING	
A. Understanding starts with an analysis of the problem	Opening quotation or other appropriate introduction
Significance of small business in American economy	
Difference between administration and operation	
Some characteristics of small business that may be a source of problems or may develop into problems	Quote Dr. A. M. Woodruff, this manual, page 15
1. Problems may result from characteristics of small-business entrepreneur:	
a. Independence -- A desirable trait but one which needs tempering with a realistic acceptance of interdependence	Read aloud from Kelley and Lawyer, page 24, or from this manual, page 16 Discuss the "my own business is my own business" attitude
b. Enterprise -- A desire to put one's own ideas or abilities to use	Refer to SBA-MRS No. 63, April 1962, Small Business Problem Studies, "Patterns of Conduct" section

Good as long as ideas are valid in terms of long range effects - - and where abilities are varied and sufficiently balanced to meet all demands upon them	Discuss Dun & Bradstreet finding - 52% didn't want any outsider involved
c. Domination as much by personal and family consideration as by impersonal profit-making motives	
(1) Hiring relatives (2) Buying from friends (3) Locating on basis of personal convenience or mere availability (4) Mixed with family finance (5) Other	Cite or have group members suggest examples
2. Problems that result from environmental factors	
a. Business operates in a non-static environment	Discuss idea of "flowing stream" in business affairs
b. Locating in inappropriate areas	
(1) Too much competition (2) Lack of affinities with surrounding businesses (3) Business dried up in a declining area or neighborhood	Quote from SBA publication The First Two Years, pages 42-49, or this manual, pages 18 and 19

c. The course of wisdom:- The small business man who hopes to survive will:	
(1) Recognize the limits of his own resources and abilities	
(2) Base business decisions on business considerations	
(3) Constantly study his business environment and the ways he can adapt to it	
3. Problems that result from inexperience	
a. Most failures are management failures	
(1) Difference between operational and administrative management skills	Experience of World War II veterans
	Dun & Bradstreet reports each year the same failure causes
(2) Persistency of same failure factors	
b. Over 90% of failures stem from management deficiencies	Visual #1
(1) Neglect, Fraud, and Disaster are management related factors	Briefly show visuals #2, #3, #4. These are management failures too, but will be dealt with more fully in subsequent presentations
(2) Specific management failings	
(a) Inexperience in line	Visual #5 -- Cases & Implications
(b) Inexperience in management	Visual #6 -- Cases & Implications

(c) Unbalanced experience	Visual #7 -- Cases & Implications
(d) Incompetence	Visual #8 -- Cases & Implications
(e) Total 92%	Summarize with Visual # 1
II. OTHER FAILURE FACTORS	
A. Recognizing the Common Pitfalls	
Underlying factors:	
1. Time to perform all the managerial functions	
2. Versatility is demanded by the lack of internal resources and specialized talent	
B. Contrasting management outlook of a big and small business	
C. Dun & Bradstreet Report Perennial Findings:	
1. Lack of Sales	Visual # 9 - Cases & Implications
2. Competitive Weakness	Visual # 10 - Cases & Implications
3. Poor Credit and Collections Policy and Procedure	Visual # 11 - Cases & Implications
4. Excessive Fixed Assets and Top Heavy Operations	Visual # 12 & 13 - Cases & Implications
5. Inventory Troubles	Visual # 14 - Cases & Implications
6. Poor Location	Visual # 15 - Cases & Implications

III. SUGGESTIONS FOR SUCCESS

A. "Keep thy shop and thy shop will keep thee."

Stress and summarize - write on blackboard
<u>ENTERPRISE</u>

B. Get some experience in the line

<u>EXPERIENCE</u>

C. Get yourself a No. 1 Boy

<u>DEPTH AND MANAGEMENT SUCCESSION</u>

D. Control your inventory and you control your business

<u>INVENTORY</u>

E. Failures are more frequently caused by people than by events -- train your people

<u>HUMAN RELATIONS AND TRAINING</u>

IV. IMPORTANCE OF GOOD MANAGEMENT TO SMALL BUSINESS

A. Underlying differences between large and small business

1. Large business has management in depth

2. Small business relies more heavily on "single level" management

3. Individual management mistakes are seldom fatal to large business

Cite example - Ford Motor Co., the Edsel

4. Single management mistakes may close a small business

B. Big advantages of Small Operators

Correctly managed, a small business can make a distinct advantage of its size

1. Simplicity - The owner puts on his thinking cap and the board of directors is in session

   Have group cite examples

2. Flexibility - On-the-spot decisions

3. Personal Relationship - The owner of small business has an opportunity for "first name" relationship with customers, suppliers, and employees

V. ONE THING MORE -

"Independence for the sake of independence"

Small-business man has many bosses

Small business Patterns of Instability

Quote Paul W. Paustian and John Lewis, Jr., SBA-MRS No. 63, Small Business Instability and Failure, 1963. This manual, pages 33 and 34.

VI. MANAGEMENT IS EASIER WHEN YOU KNOW HOW

A. Five underlying functions which constitute the foundation of a good management approach

1. <u>Planning</u> - Policies and procedures

   a. Handling change and competition

   b. Projecting the future operation on the basis of past history, records, etc.

   c. Check planning with why, who, when, what where, and how

2. Organizing - Duties, positions, staffing

   a. Setting up organizational structure

   b. Determining jobs to be done, lines to be carried, services to be rendered

   c. Prepare job analyses for each phase of operation and each <u>key</u> position

   d. Establish operational and control policies

   e. Select, train, and allocate personnel

3. Directing - Leading, motivating, delegating

   a. Assignment of duties, listing responsibilities

   b. Varying emphasis by special assignment

c. Giving orders: verbal for emergencies or	Cite examples
simple orders; written for detailed, long orders	Cite examples
d. Good directing founded on good organization which provides	
(1) Unity of command -- one boss	Cite importance in small partnership situations
(2) Span of control -- no more than one man can handle	Cite examples
(3) Homogeneous assignment -- similar functions in one job (departmentalization)	Cite examples
(4) Delegation of authority -- if a man has responsibility, he also needs authority to carry it out	Cite examples
4. Coordinating - Accomplishing group objectives	
a. Interpret plans, policies, regulations	
b. Train in groups and individually	
c. Contact coordinate groups and persons	Cite examples
d. Follow-up in conferences and meetings	
5. Controlling - Measuring and correcting	Cite examples

a. Set up required controls	Cite examples
b. Determine standards	
c. Check results	
d. Correct - retrain	
e. Appraise and control cost - quality - production and sales	
VII. PREREQUISITES FOR SUCCESS Existence of a real business opportunity Management ability and background Adequate capital and credit Modern methods Insurance against measurable risks Management philosophy	
VIII. YOU CAN LEARN - WHAT AND HOW	
A. Are You Qualified To Learn	Relate story of Epictetus (Eṕ-ick-tee-tus) or other appropriate introduction
One learns by: a. Personal experience b. Experience of others	
c. Trade associations and press	Discuss pros and cons
d. SBA - DE co-sponsored management courses	
B. Close Session	

SUCCESS AND FAILURE FACTORS IN SMALL BUSINESS

MANAGEMENT IS EASIER WHEN YOU KNOW WHAT YOU'RE DOING

Did you ever hear someone make a statement like this? "Don't bother me with the details, I've already made up my mind." For some businessmen it represents an attitude that is all too common. Small-business failures have been reported so often and sometimes so dramatically that many people believe that the small-business operator doesn't have a chance in the highly competitive economy of today's market place. They make conclusions on the bases of generalizations.

"The big fellows control this or that area of business."

"There's no room for the little independent guy."

"The man with an idea or a dream might just as well forget it, put on a grey flannel suit, buy himself a brief-case, a pair of sunglasses, and become an organizational man in a large corporation."

Thus many a potential independent operator is dissuaded from entering the field of small business, and many managers give up after a brief trial. Too often, as the "slogan" suggests, we find that we have already made up our minds before we have examined the specific details of the problem.

However, it can be easily established that the vast majority of small-business failures are the result of mismanagement or uninformed management rather than relative size or competition. This presentation will stress management hazards and cite the high percentage of independent businesses that fall by the wayside because they fail to recognize their problem until it is too late. Each year on the national scale we witness about 440,000 "starts" and about 400,000 "closures" or discontinuances of small operations. This leaves us a net gain of just 40,000 or about a 9 percent growth factor over starts. (This represents less than a 1 percent increase in the total number of businesses.)

Not only does this constitute a lot of individual problems or headaches for the 400,000 "closures," it is also the source of a big collective headache in our national economy. Many people, including many of those engaged in independent business, regard the contribution of the small firm to our national economic life as being insignificant and unimportant. Nothing could be further from the truth. It has been reported that:

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95% of all businesses in America are "small" businesses;

40% of our total business volume is done by small firms;

40% of our working force is employed in small enterprises.

These figures, properly understood, bring home a truth that is most significant to every American. Small-business hazards and closures are more than statistical quotations. They are more than the unforeseen or unrecognized problems of a few victims of their own short-sightedness or inexperience. They are lost jobs and lost growth in our national productivity; they are unfired weapons in the cold war; they are American men and women and their families who are forced to live below our national economic standard of living.

All this, we shall see, is not due to a lack of technical know-how in the various fields of business endeavor. Only rarely does one trace a failure of an independent electronic enterpriser purely to a lack of knowledge of the field of electronics, of a food distributor to inadequate understanding of the food trade, or of a contractor to inexperience in the building trades. Where these conditions exist at all, one will generally find them combined with the "great failure of being unable to recognize the problem." This is another way of saying they are lacking in "management know-how." Consequently, this and subsequent presentations will make a distinction between "administrative management" and "operational know-how." When I use the term, "management," I shall mean administrative, general, or top management.

Operations are diverse and frequently individualized, especially in smaller concerns. We cannot and do not pretend to bring you, or even to know, the intricacies of the myriad of complex operational factors involved in the varied fields represented in this group. But the principles of good administration are universal. Administrative management is the bigger problem. If you have an operational problem, you may actually find that it is "a problem within a problem." By attacking the larger management problem first, you may be reducing or eliminating many of your other headaches. We propose, therefore, to hit and hit hard at the various management failure factors that have popped up with such a persistency that they could almost be codified as an index of, or a road map to, foreclosure. We do not expect any of you to take that road. That is why we shall post the warning signs with such prominence that some of you might get the feeling they are almost blatant. If we "rattle the coffin," so to speak, it will be because we don't like and can't afford funerals in our economic life.

Business consultants, educators, and Small Business Administration financial and management personnel all agree that the problems which the small-business man brings to them are usually not the basic problem; they are frequently the superficial irritations that are indicative of an underlying malady or weakness. For example, a small-business man sees his problem as the new competitor across the street while in reality his business is sick because his expenses are too high as a result of not controlling his business adequately. We shall try to probe deeply enough to uncover the real rather than the surface problems involved.

PROBLEMS CAN RESULT FROM PERSONAL CHARACTERISTICS

Part of the difficulty independent business men have in recognizing their real problem is the fact that they are frequently so close to it, so wrapped up in it, so to speak, that they feel its effects without knowing it exists. There's an old wall motto which every small-business man would do well to place on his desk or wall. It poses this question, "ARE YOU CONTRIBUTING A SOLUTION--OR ARE YOU PART OF THE PROBLEM?"

The small-business manager who is honest with himself will, if given adequate time for reflection and self-appraisal, come to the conclusion that he is indeed a part of his own problem.

In a discussion of "Causes of Failure" presented to the membership of the conference on "The Problems of Training Small Business Executives" conducted at the University of Colorado, Dr. A. M. Woodruff, Dean of the School of Government, Business, and International Affairs, George Washington University, Washington, D. C., made the following statement:

> "The management of small business is (frequently) in the hands of men who are the unreconstructed rebels of the business world. They are free from the prefabricated inhibitions which are impressed by the giant stamping mills that turn out the junior executives of large corporations, and I could name them, all of whose junior executives of a certain level look alike, dress alike, walk alike, and think alike. This is not true of small businesses. These fellows are rugged individuals. Always remember this, gentlemen, when dealing with them and trying to educate them because you've got to deal

with them on this basis."

This statement tends to glorify the small-business man as the inheritor of a beloved American tradition, and as perhaps the vestige of a vanishing type in our society. But it also poses something of a problem. Pearce C. Kelley and Kenneth Lawyer in their book, How to Organize and Operate a Small Business, list three characteristics of small operators which may throw some light on the situation we are trying to bring into focus.

1. He has a highly developed sense of independence--or at least a strong desire to be independent of outside control.

2. He has a strong sense of enterprise--or a desire to put his own ideas and abilities to effective use.

3. He may be as much dominated by personal and family considerations as he is by impersonal profit-making motives, both in launching and in conducting his own business.

Oddly enough, this very independence and enterprise of the small entrepreneur can be, and frequently is, as much an "Achilles' heel" as it is a bulwark. Harry M. Meacham, a former Dun & Bradstreet, Inc. executive (now retired), and a strong advocate of administrative management training as opposed to mere operations, was untiring in his admonitions to the small-business man. In a TV presentation in Hagerstown, Maryland, he stated:

"What of the casualties? Which are the failure-prone marketers today --here in this area--perhaps within range of my voice?

"Thousands of small businesses, which today are flourishing, have within them the seeds of destruction. This may be a fatal flaw in the character or mental equipment of the owner . . . Prominent among the likely casualties is the know-it-all.

"Dun & Bradstreet is always making surveys and feeling the business pulse. Not long ago we asked a cross section of small-business men if they would accept outside assistance or advice. A majority (52 percent) said they didn't want advice from anybody. Outsiders, they said, are long on theory and short on practice. (By outsiders they meant their banker, their accountant, their government and their suppliers.) No, they'd make their own mistakes.

"And they will--no doubt about that. It has been reported that 75 percent of these small-business men overpay their taxes--because they won't accept advice.

"Rugged individualism is fine--up to a point. We admire the marketer who refuses to accept a crutch or cushion. But we criticize him for refusing to accept a light to guide his steps. Yes, Mr. Hardhead is a candidate for the bankruptcy courts."*

*Underscoring added.

Closely associated with the small-business man's independence is his sense of enterprise. Some don't have enough of this commodity while others, it would seem, have too much. Both extremes constitute an element of danger. Risk-taking and adverturing are necessary elements in the make-up of an enterpriser, but there is a wide gap between risk-taking and gambling. The biggest risk-takers in the world are insurance companies -- but insurance companies don't gamble. They carefully examine all the facts, compare these facts with scientifically developed mortality tables, and then project a line of action which insures a return on their investment. The gambler, on the other hand, relies on chance. The small-business man who tries to do everything by himself, or who operates "by the seat of his pants" is inviting disaster. At best he can generally expect to barely scrape along. At worst, he can lose his business, his shirt, and, perhaps, his self-respect.

Kelley and Lawyer point out a third characteristic of small operators that may contain another seed of destruction.

"In many small concerns," they say, "personal factors, usually non-financial, dominate the impersonal profit-seeking motive." These include community and family ties, the age, health, and general outlook of the would-be managers.

Larger businesses tend to base decisions purely on business considerations, while the small operator may be so involved in these personal factors that he puts them above purely business considerations. Case histories abound of businesses that have been ruined by the complications of a manager's family life. There's the brother-in-law who is a bum and an incompetent, but it's cheaper to bring him into the business than it is to support him. There's the "big order" that goes not to the best qualified supplier, but is shunted over to Cousin Harry who has been having a rough time keeping his raccoon coat operation going ever since the "Stein Song" went off the Hit Parade. There's the family budget that never seems elastic enough to stretch from Monday to Saturday, making it necessary to "draw" a few bucks out of the business.

We are not saying that any of these situations should be ignored, but we are certainly on solid ground in pointing out that the business man who regularly follows such a line of conduct is in training to become a business mortality statistic.

PROBLEMS CAN RESULT FROM ENVIRONMENTAL FACTORS

An old Greek, of about 2500 years ago, is credited with developing, what we might call, the theory of "tides" in human affairs. Everything flows, he suggested, so that it is impossible to swim in the same stream twice. Shakespeare extends this thought with his famous quote, "There is a tide in the affairs of men, which, taken at the flood, leads on to fortune."

The stream the small-business man must swim in, and tides which carry him to success or failure, are the variety of geographic, economic, and personal factors which constitute the environment in which the business is trying to operate.

A most readable and informative book has recently been published by SBA which focuses new light on these and other small-business factors through the device of case histories of 81 small retail and service firms over a two-year period. The book is called, The First Two Years: Problems of Small Firm Growth and Survival. More will be said about this book later in this presentation and in subsequent sessions, but for the moment we would like to give you just one quote:

> "The choice of location (geographic - social - economic patterns) was frequently based on such reasons as vacancy of premises, nearness to home, familiarity

with the neighborhood, and availability of a business for sale. Too often these reasons appeared to the owners as good and sufficient; they did not bother to make any objective evaluations of the locations' potentials as business sites. Failing to do so, some overlooked the fact that the area was declining, that is, losing population or being by-passed because of new highway construction, or that it was unsuited for the type of goods or services offered. In some instances, the business was too specialized, and in others, the same goods or services were already adequately supplied by different firms."

The report goes on to indicate that within two years, 40 of these 81 firms had closed their doors while others were "marginal closures"; that is, they should have been closed by all rules of economics and logic but were being held together by a combination of bailing wire, tenacity, and stamina. Geography and other environmental forces were not the only, or even the dominant, factors in these failures or "still births," but they certainly played a part in the cases studied. It might be said that some of these "merchants" were trying to navigate a tide that was too full or too turbulent for their delicate crafts, while others were trying to swim in a stream that had already dried up.

Borrowing another idea from Harry Meacham, we can sum up these observations with a little story from Greek mythology:

In an apocryphal debate between Homer and Hesiod regarding the identity of the wisest man in the world, Hesiod asked the blind Homer, "What is the mark of wisdom among men?" and Homer replied, "To understand the present and to plan for the future."

The small entrepreneur who hopes to survive and prosper must:

(1) Recognize his own assets - and his liabilities or short-comings and seek and accept outside help when it is needed or dictated by common sense.

(2) Base business decisions on business considerations.

(3) Understand his business and the factors working in and around it.

PROBLEMS CAN RESULT FROM INEXPERIENCE

Today the order is change -- adapt or perish. Change and adaption require skill and technical know-how. We know that rapid business changes and fluctuations result in increased business mortality which is the usual effect of unskilled, misinformed, inexperienced or otherwise incapable management.

At this point, it might be well for us to indicate a rather fundamental distinction that is all too frequently overlooked or ignored by small-business men. There is a difference between technical or operational know-how and managerial skill. After World War II, thousands of ex-GI's who had received the finest technical training in such areas as electronics, construction, logistics, and distribution, and who found ready financing via the GI Bill, decided to "become their own bosses" and ventured into an independent operation. Some of these businesses blossomed and are now bulwarks of their communities. Others unfortunately folded with heavy losses. The basic difference between the two groups was the perennial problem between operating and managing.

Going back to Dun & Bradstreet's analysis of business failures, one may observe an eternal persistency of the same failure factors year after year after year. Dun & Bradstreet has reported and analyzed hundreds of thousands of business failures over the years. The same basic reasons cause these failures.

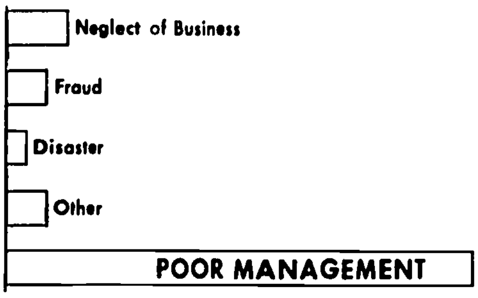
MANAGEMENT FAILURES

Inexperience in line	9%
Inexperience in management	18%
Unbalanced experience	20%
Incompetence	45%
	92%

These four management causes of failure will be further elaborated upon in a moment, but at this point we merely want to show the high percentage of failures that are the result of poorly prepared, poorly informed, or poorly organized (or disorganized) management.

Although itemized separately, the other 8 percent of failure factors can, in most cases, be traced either directly or indirectly to poor management. These include:

CAUSES OF BUSINESS FAILURES



3% Neglect (which is really a neglect by management)

2% Fraud (which may be a fraud in which management is involved or at least failed to guard against)

1% Disaster (which management did not secure itself against by insurance, protection, etc.)

Three hundred years ago, John Donne, the Elizabethan poet, said, "Any man's death diminishes me, because I am involved in mankind." So every business failure diminishes the total business and economic structure of the community.

Failures resulting in loss to creditors (and so directly effecting members of the community other than the bankrupt businessman and his family) totaled 14,374 in 1963. This was a national failure rate of 56.3 per 10,000 starts. This is not a significant figure in terms of the economy of the nation as a whole, but it is highly significant to the 14,374 businessmen involved, to their families, their employees, their creditors, and their customers.

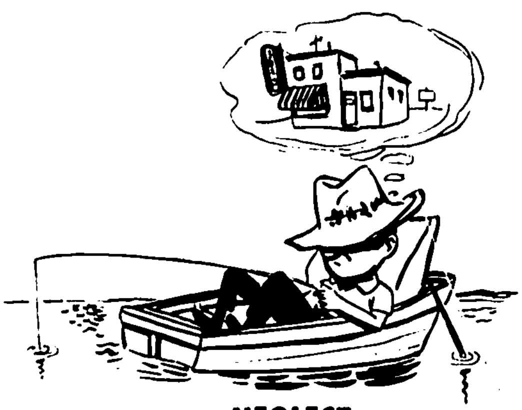
Moreover, when it is realized that this figure included only those business closures which resulted in loss to creditors or were otherwise "forced" by circumstances or the bankruptcy court, the figure picks up new importance. For every such business that closes with losses to outsiders, there are undoubtedly many additional business failures where the losses are withstood quietly by the owner and his family.

Why do some 14,000 businesses fail annually? Why do they die? What can we learn from their autopsy? Let's look at some statistics.

NEGLECT

About 3 out of every 100 failures result from neglect. Neglect stems from bad habits, poor health, marital difficulties, complacency, or laziness. Most of these failures could be avoided.

All too often one sees a young man start a business with every expectation of success: training, location, capital, a desire to excel. There seems to be every reason to assume that here is security and



NEGLECT

stability for a family, education for children, and the chance to perpetuate a vision and a name.

Then the owner becomes complacent. He begins to spend too much time "entertaining customers" on the golf course, or looking for new prospects at the seashore. He begins to drink too much, develops a "wandering eye" . . . and his monument begins to crumble before it has had a chance to be inscribed with the "And Son" inscription.

Neglect is worse than poor management -- it is no management at all. Eternal vigilence is the price of survival. Three hundred years ago George Chapman said, "Keep thy shop and thy shop will keep thee." The admonition is valid today.

Since the matters of Fraud and Disaster will be covered more fully in a later presentation of this series, we merely indicate them at this point for statistical purposes. (Visuals 3 and 4)

LACK OF EXPERIENCE IN THE LINE

LACK OF EXPERIENCE IN THE LINE

You may draw on the records as well as numerous personal observations to develop a host of convenient illustrations to dramatize this point. Time, however, limits us to a single case history. You can undoubtedly suggest others from your own observation or community history.

This case points up the fact that a man can be a great success in one line of business endeavor, and an utter hazard to himself and others in another line in which he has had little or no prior experience.

Our case involves a merchant who had made a substantial fortune in the wholesale food business. In fact, he was so successful that he was able to retire at 50, an age at which the average businessman is just beginning to mature businesswise, and -- so to speak -- get his second wind. In a magnanimous mood and in recognition of the share his employees had had in making him the success he was, he gave the enterprise -- lock, stock, and barrel -- to his long-time associates.

After several years he became restless and bored with his self-enforced leisure and decided to get back into the business whirl.

But did he go into the food business which he knew from A to Z? No indeed, that was "old hat" to him, and he was so full of vigor that he wanted the challenge of the unknown -- so he went into a manufacturing line where he lost every cent he had in the world and ended up clerking in the wholesale food warehouse he had founded.

He had forgotten the long years of apprenticeship he had served as a delivery boy, clerk, and salesman. He thought that success in one line was his assurance of success in any line. He was wrong.

LACK OF MANAGEMENT EXPERIENCE

A manufacturer in North Carolina had built up a very nice business, netting over $100,000 a year. After his son had finished college and done his Army stint, he came into the shop. He was "trained" for about three months, whereupon "Pop" turned the operation over to Junior, and headed for Europe. For a year or so thereafter Pop traveled, dabbled in politics, and lived the life of "Riley" attending fraternal conventions and nocturnal wing-dings. He never had so much fun -- or so he thought -- in his entire life. But about this time he dropped around to take a look at the operation. It was now losing $100,000 a year. More than that, competition had caught up with him. And so, in his twilight years when he should have been taking it easy, he's doing what he should have done years ago -- he's trying to make a manager of his son.

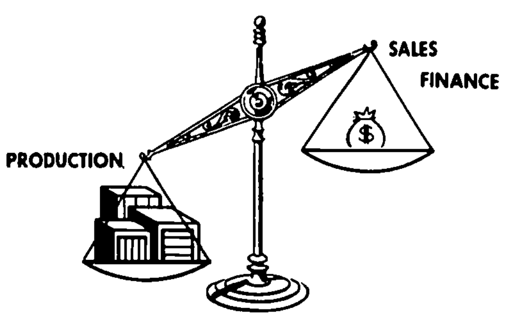
This case points up two important lessons:

1. Management training -- or the lack of it -- can be of paramount importance.

2. Failure to bring young people along in the business -- which is actually failure to prepare for a continuation of knowledgeable management -- is one of the fundamental reasons why some firms remain small -- or disappear.

LACK OF MANAGEMENT EXPERIENCE

UNBALANCED EXPERIENCE



UNBALANCED EXPERIENCE

Almost 20 out of 100 management failures stem from lack of well-rounded experience in buying, selling, financing, controlling, and production.

Suppose a man's personal interest and experience lie in production. He spends the bulk of his time in the shop -- overproducing. In the meantime, inventory piles up; and selling, recordkeeping, and cost control are left to chance, while he keeps producing -- at a loss.

We'll see later that large corporations have a key man -- or men -- for every key job. On the other hand, the small marketer must wear all the hats -- and some of them don't fit any too well.

So here's a tip for survival -- develop your versatility.

SUCCESS AND FAILURE FACTORS

A small-business manager faces two problems that are the peculiar characteristics of small business.

The first is the problem of time -- time to perform effectively all of the management things that management should be doing. The second is a problem of ready access to and use of authoritative information -- rather than managing by the crystal-gazing process of "by guess and by golly."

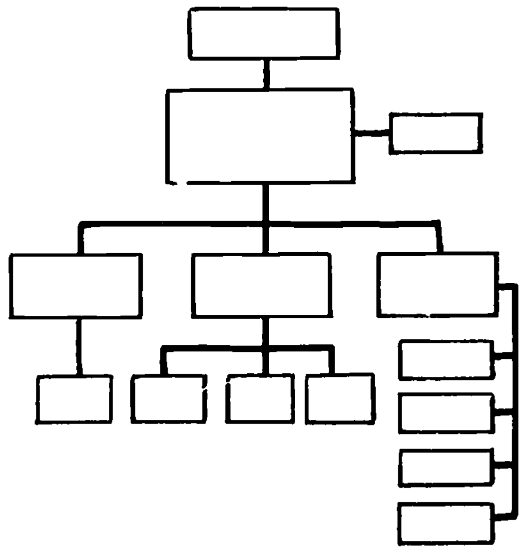
We introduced the idea of versatility a moment ago. Do you know that, as a small-business manager, you have to be much more versatile than the manager of a large organization?

Large business has almost unlimited internal resources and specialized talent available for every conceivable situation, emergency, or exigency.

LARGE BUSINESS HAS MANAGEMENT IN DEPTH

There is:

The Chairman of the Board,
The President,
The Administrative Assistant to the President,
The Vice President for Financial Affairs,
The Vice President for Legal Affairs,
The Vice President in charge of Personnel,
The Vice President for Operational Affairs,
The Assistants to the Vice Presidents,
Etc.,
Etc.,



In small business, on the other hand, there are generally very limited internal resources, and one man wears all the management hats.

He is:

Boss,
Office Manager,
Production Manager,
Sales Manager,
Treasurer,
"Sea Lawyer,"
Financial Analyst,
"Head Worrier,"
Etc.,
Etc.

It is no wonder that some small-business managers are occasionally accused of crystal-gazing.

It might be fruitful if we compare the day-to-day, crisis-to-crisis, hand-to-mouth thinking of many small operators with the management attitude of the larger firms around them. At this point it is safe to state that perhaps the reason some businesses have gotten big is because they have habitually done most things right.

INCOMPETENCE

INCOMPETENCE

The dictionary defines "an incompetent" as "one incapable of managing his (own) affairs." Almost half of the businessmen classified as failures should never have engaged in private business at all, because they are incapable of "managing affairs" -- or in blunter terms -- are <u>incompetent</u>.

This is bad, but one quick cure -- a controlled economy -- would not only kill the given patient, it would also cause the demise of our free, competitive economy, in which a man is free to enter business, is free to succeed, free to fail, if need be, and even free to try again.

BIG AND SMALL BUSINESSES HAVE CONTRASTING OUTLOOK

The little fellow says, "Let tomorrow take care of tomorrow. I have my hands full today."

The big fellow budgets and otherwise plans ahead a minimum of three to four years.

The small owner-manager says, "Why should I teach anybody what I know, and create a possible threat, when I'm running the business and making a few bucks?"

The large businesses are keenly aware of the need to operate a management development program. The hiring of young people as management-trainees, in actuality, constitutes collecting a pool of potential management talent that may be used to meet future needs.

We're not confining these examples to the industrial giants like U. S. Steel or General Motors. There are businesses all around you with three to ten employees -- and not one of their employees trained to take over in an emergency, or to relieve the manager so that he can attend a trade meeting or a management course such as this one.

Here are some of the contributory causes of the management failures just reviewed. These strongly indicate that the small-business man must develop specialized assistants if he hopes to grow, or even to stay in business. In big business, mistakes that are not caught by one or the other of the levels of management are at least absorbed, and the shock is so distributed that it has only temporary effect on business. In the case of the smaller operator, a single mistake might be the one that calls in the undertaker or mortality statistician.

LACK OF SALES

Lack of balance between sales and other phases of the business means that someone is asleep on the job. There is a lack of coordination.

INADEQUATE SALES

Sales, of course, go much deeper than mere point of sales contact. N. H. Ringstrom, head of the Marketing Department at Oklahoma State University, may have been referring to a particular trade in the following quote from his SBA Management Research Summary, Small Business Success and Failure Cases, but the implications are there for all small businesses to draw on:

> "In addition to areas already discussed, the successful dealer . . . is skilled in (1) proper use of advertising and other types of sales promotion; (2) selection of merchandise his customers like; (3) the pricing of this merchandise, not only at profitable levels, but also at figures customers are willing to pay; (4) provision for good customer service; (5) proper selection of store location and good use of store layout; and (6) the institution and use of internal controls, including cost accounting."

Of course, Dr. Ringstrom's points overlap with other activities; but they are all sales-connected functions which have a direct bearing on point-of-sale success or failure. These functions, incidently, will be more thoroughly discussed in later presentations of this series.

COMPETITIVE WEAKNESS

COMPETITIVE WEAKNESS

You can't expect to operate a hamburger stand next to the Waldorf Astoria and charge its price for your blue-plate special. Too many businessmen try to deal with competitors by cutting prices. Generally they end up by cutting quality or service, and eventually eliminating profit.

Almost half the management failures, traceable to competitive weaknesses, occur because owners were unable to overcome the increased costs resulting from competitive action. In the long run, competition tends to reduce costs by bringing about increased efficiency among the survivors. Businessmen say that the best way to solve this problem is by:

1. Reducing expenses.
2. Increasing sales.

There are many ways to reduce expenses but some, such as cutting quality below an acceptable standard, elimination of training programs, and the hiring of "cheap" help, may prove costly in the end.

Reduction in expense without substantially cutting into quality or service is only possible when a more efficient production and a better selling job is done. Both of these desirable ends are the direct objectives of training. Trained people reduce supervisory cost, sell higher-profit items, upgrade sales, reduce the number of lost orders, hold down credit losses, and contribute to the prestige of the business in a way that cannot be duplicated.

We shall have additional comments on salesmanship and sales training during subsequent sessions of this series. At the moment, however, we'd like to point out that sales training can be custom-tailored to your kind of business through various programs of administrative and operative management offered by Distributive Education, trade organizations, and local schools, universities, and colleges.

Before we leave this subject of selling, we should point out that surveys show that within a ten-year period, the average small business loses 80 out of every 100 customers it serves. Customers leave for a variety of reasons (many of which could be avoided):

Poor service,
Indifference,
Failure to settle grievances,
Lower prices elsewhere,
Influenced to trade elsewhere,
Moved or died.

We can't do much about the last classification, but you might be shocked to learn that nearly 70 percent of customer losses are directly traceable to indifference or poor service on the part of business. Obviously customer retention, replacement, and acquisition is a major part of management's job. It is generally conceded that the manufacturing industry is decades ahead of retailing and service businesses in the scientific approach to this important management responsibility.

CREDIT AND COLLECTIONS

Business is dependent upon a constant flow of capital. Stock is purchased and sold. If a business is to pay its own bills regularly and make a profit, it must in turn receive prompt payment for the goods it sells or the services it renders. Many small businesses get into "hot water" because management is so eager to make sales and build customer satisfaction that collections become a slow and painful process of "wishful waiting." All of the sales in the world won't keep a business afloat if payment is not forth-coming. It is easier to maintain customer satisfaction with a reasonable system of prompt collections, than it is to extend unwarranted credit.

POOR COLLECTIONS

About 10 percent of failures can be located in the credit department. The road to failure through receivables difficulties is clearly marked. Just read the signs:

1. Lack of a clear-cut credit "policy,"

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2. Haphazard collection procedures, and

3. Loss of your own discount because you can't meet contract terms for lack of cash on hand.

EXCESSIVE FIXED ASSETS AND TOP-HEAVY OPERATIONAL EXPENSES

EXCESSIVE FIXED ASSETS

Excessive fixed assets or too much building, equipment, and land investment, combined with top-heavy operational expenses (payroll, supplies, and transportation), put a small business in a most hazardous position. As an example, transportation may be an essential expense, but transportation to the golf course might be a one-way ticket to the bankruptcy court. Almost 7 percent of small businesses fold up because their money gets all tied up in equipment. A recent business obituary revealed that a young man started out under the most favorable conditions:

Adequate training,
Sufficient capital,
Good location, and a
Competitive product.

TOP HEAVY EXPENSES

Yet he failed within six months because he spent too much on flashy fixtures, a high-priced car, and a mahogany-paneled office -- all of this for a variety store in a small town. It could have been a most profitable enterprise, but this is a shirt sleeve kind of business that cannot be operated by a man in a tuxedo from behind a six-foot polished mahogany desk.

INVENTORY TROUBLE

INVENTORY TROUBLE

Have you ever been tempted to heavily overstock a particular item -- just because somebody is anxious to make you a "deal"? Be alert to opportunity, but remember that behind every bargain there is some kind of story. Eight out of 100 failures are the result of poor judgment in buying. Many small businesses fail to make full use of their service wholesaler. Watch out for quantity purchases which you cannot sell or use within a reasonable period. You may not realize it because you don't actually see the cash going out, but it is costing you money just to hold such nonmoving items in stock. If you were to prorate your rent cost according to stock lines, you would get a true picture of what kind of a bargain you got when someone unloaded that slow-moving merchandise on you.

LOCATION

POOR LOCATION

We have already alluded to the fact that all too frequently in small business the matter of location is determined to a large degree by non-business considerations. This sometimes results in the business being originally located or remaining in an area from which a substantial portion of its market has departed. About 2 percent of failures, year after year, result from "location problems." In a somewhat exaggerated example, Joe has a haberdashery in the desert -- but a shopping center full of haberdasheries might be an even worse location. If you are starting a new enterprise -- or opening a branch -- study locations and relate them to your enterprise. Certain businesses have "affinities" for each other; that is, they act like magnets by drawing in mutually profitable "traffic." Restaurants, theaters, and supermarkets, for example, draw people who stay a while and shop a whole area. Service stations, wholesalers, and construction firms tend, on the other hand, to bring only touch-and-go traffic. Study affinities.

IMPORTANCE OF GOOD MANAGEMENT TO SMALL BUSINESS

Having pointed out the more common hazards of business and, we hope, having convinced you that failures are caused by people rather than events, we would like now to move on to a more positive aspect of the picture.

We have to some extent outlined the differences in management approaches and management problems between big and small business. It might be well to restate four basic points:

1. Large business has management-in-depth.

2. Small business relies more heavily on single-level management.

3. Individual management mistakes are seldom fatal to large businesses.

4. A single mistake on the part of a small-business man may result in closure of the firm.

But let us not get the impression that big business has all the advantages. Increased size may improve efficiency up to a certain point, but beyond that point, size can become a disadvantage. Big business can become ponderous and slow-moving, while small business, competently managed, can make a distinct advantage out of smallness. Factors on the plus side for properly controlled small business are:

Simplicity - The owner puts on his thinking cap, and the board of directors is in session.

Flexibility - He can make on-the-spot decisions in the time it takes a supervisor in the large firm to get an appointment with his own boss.

Personal Relationship - The owner of the small business can get to know the first names of his customers, what they are buying, and what they are thinking.

These factors can only be developed into positive business assets by management that is aware of the management function as opposed to the operational function, and which is prepared to use the principles of scientific management in combination with flexibility, simplicity, and personal touch.

ONE MORE THING

We must honestly face the fact that the operation of an independent enterprise is probably the toughest line of endeavor an individual can undertake. The fellow who merely desires "independence for the sake of independence," or whose sole reason for going into business is to be his own boss, might be sorely disappointed. The independent entrepreneur probably has more bosses than he realizes. These are:

1. The local, State, and Federal regulatory bodies,
2. The resource agencies or suppliers who control material flow, and sometimes storage, credit, and sales policy,
3. The financial backer and creditors,
4. The customers,
5. The demands and cycles of the market itself, and
6. The demands on the manager's personal life.

All of these call for a mature, balanced personality and an aggressive, diplomatic character. Independent business is not the place for the weakling or the person determined to take it easy. Paul W. Paustian, Professor of Economics, and John E. Lewis, Jr., Research Associate, University of Alabama, in an SBA Management Research Report, Small Business Instability and Failure, list certain "Patterns of Instability" which include these characteristics of weakness:

Failure of operator to keep his head in a crisis,
Personality deficiencies of the owner,
Tendency toward short-run maximization,
Inability to adapt to changing conditions,
"Hibernation" rather than failure,
Laziness of operator or owner,

Unjustified cash drain in the form of salary,
Imprudent extension of credit, and
Operation of the business as a sideline.

Also included in any listing of advantages and disadvantages, or large versus small contrasts, are the following not insurmountable factors affecting the small-business man:

1. Independents can't get quantity discounts and other buying economies -- unless they join buying groups.

2. Independents are limited financially in meeting chain competition in such areas as advertising and sales promotion -- unless they form cooperative promotional groups or are in effect franchised dealers relying on supplier promotion.

3. Independents are limited in their opportunity to experiment with products, services, or techniques since they can't spread the risk as thinly as larger organizations.

4. Independents frequently are limited by size to the processes, techniques, and equipment they may use or can afford to use.

A careful consideration of all pertinent factors is dictated both by the very nature of small enterprises and by common sense.

MANAGEMENT IS EASIER WHEN YOU KNOW HOW

This entire series of presentations is intended to provide a channel for the exploration of the various aspects of management know-how. At the moment, we will content ourselves with five underlying functions which constitute the foundation of a good management approach. These are planning, organizing, directing, coordinating, and controlling; and, briefly outlined, they should cover:

A. Planning - Policies and Procedures - Handling Change, Competition, Decision-Making

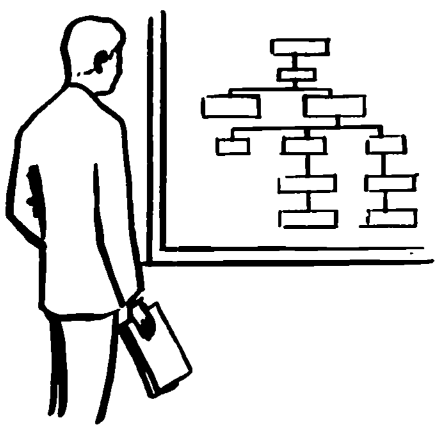
   1. Projecting the future operation on the basis of past history, records, and experience in

the existing market.

2. Check the planning process with:

Why?	What?
When?	Where?
Who?	How?

B. <u>Organizing</u> - Duties, Positions, Staffing



1. Setting up an organization structure.

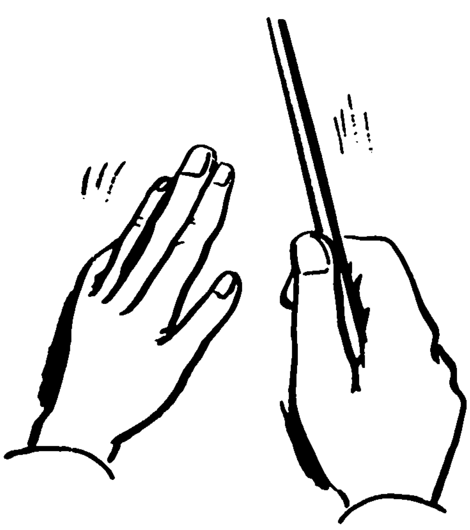
2. Determine jobs to be done, lines to be carried, services to be rendered.

3. Prepare job analyses for each phase of operation and each key position.

4. Establish operational and control policies to effectively and profitably accomplish the objectives of the business.

5. Select, train, allocate personnel.

C. <u>Directing</u> - Leading, Motivating, Delegating



1. Assignment of duties, listing responsibilities.

2. Varying emphasis by special arrangement.

3. Giving current orders. Verbal for emergencies or simple orders. Written for detailed, long orders.

4. Good directing is founded on good organization which provides:

   a. Unity of command - one boss.

b. Span of control - no more than a man can handle.

c. Homogeneous assignment - similar functions in one job or department.

d. Delegation of authority - if a man has a <u>responsibility</u>, he also needs <u>authority</u> to carry it out.

D. <u>Coordinating</u> - Accomplishing Group Objectives

1. Interpret plans, policies, regulations.
2. Train in groups and individually.
3. Contact coordinate groups and persons.
4. Hold follow-up conferences and group meetings.

E. <u>Controlling</u> - Measuring and Correcting

1. Set up required controls on such items as operational expenses, lines carried, promotional efforts, customer services, and so forth.
2. Determine standards.
3. Check results, evaluate.
4. Correct - retrain.
5. Constantly appraise and control -

   a. Cost

   b. Quality

   c. Production and sales

PREREQUISITES FOR SUCCESS IN BUSINESS

Having considered the cause of failure, it is now possible to formulate certain of the prerequisites for success.

Existence of Business Opportunity

The first prerequisite for business success is the existence of a real, not merely an apparent, business opportunity.

This means that the firm must sell goods or services needed and desired by the public.

Obviously, a small entrepreneur must first check the public need for his goods and services. Second, he must examine the available market as to sales potentials at various prices.

The elasticity of demand and the possibility of expanding sales with advertising must also be estimated.

Management Ability and Background

The second prerequisite for success in both a large and a small business is real management ability on the part of its management team or manager.

Concretely, this means skill in handling men, money, and inventories, along with ability to formulate wise policies, select proper methods, merchandise aggressively, and create good relationships with employees, customers, and the general public.

A minimum of three years' experience in the given line, or a closely related line, is recommended. Preferably some time should have been spent in a management capacity.

Now why is all of this experience needed? It makes it possible for the small entrepreneur, as well as for the big business executive, to know the tax angles, insurance needs, relationships to regulatory agencies of government, and the labor laws currently in force that are applicable to his business.

It acquaints him with operating and office methods and procedures, the need for adequate records and reporting systems, the meaning and the proper use of various controls afforded by accounting and statistics, and the importance of participation in civic affairs.

Adequate Capital and Credit

Another requirement for success is adequacy of capital and credit, together with a knowledge of how to use both properly in financing operations.

It is recommended that equity (ownership) capital be as large a part as possible of total capital invested.

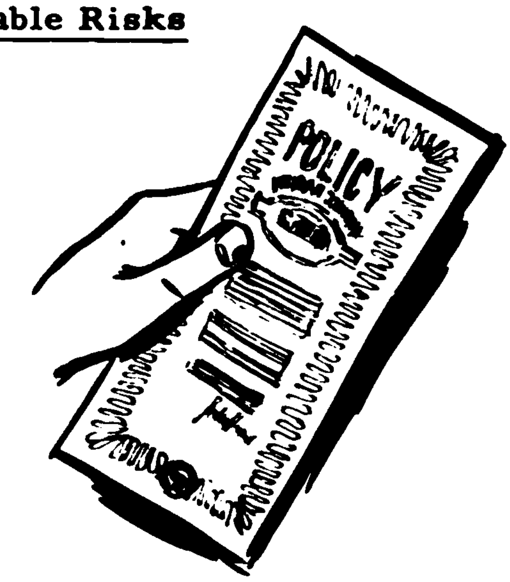
Working capital, at the inception of operations, should be sufficient to assure operations for a minimum of six months, but preferably for twelve months.

Modern Methods

Another prerequisite for business success, closely related to that of management ability, is the use of modern methods, research, and a scientific approach to solution of the problems of the business.

Insurance for Measurable Risks

A final prerequisite for business success is to identify all possible business risks and to make provision for those that are insurable by taking out appropriate insurance policies. This topic will be fully covered in a subsequent session.



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MANAGEMENT PHILOSOPHY AND BUSINESS SUCCESS

There are those in business who would scorn the notion that the managerial philosophy of those operating a business can make a contribution to business success. However, successful management has a philosophy which can be stated as follows:

1. Be readily adaptable to new methods and new products.

2. Adhere to the theory and practice of mass production for mass distribution, if feasible. For firms catering to special markets -- such as specialty grocers who sell imported delicacies only -- this is not practicable.

3. Play fair with labor, recognizing the worker as a partner in the enterprise.

4. Exercise a well-developed sense of civic responsibility.

YOU CAN LEARN WHAT AND HOW

Perhaps a number of you are back "in school" now for the first time in a number of years. It might be well, therefore, to recall a story about Epictetus (Ep'-ick-tee'-tus), a teacher-philosopher of 2000 years ago. One day one of his students asked him, "Master, why is it you never address any of your remarks to me?" And Epictetus replied, "Are you qualified to learn?" To borrow a term, one must be ready, willing and able to learn.

In this age of exploding technological and social change, specialized training is essential. One recognizes the need for apprenticeship or internship in nearly all trades or professions. Why is it that so many think they can start and conduct a business in our highly competitive economy, without study, experience, or training?

Increasing automation in the shop and office, nuclear power, agricultural and commodity production which threatens to overrun us -- how are we to learn to cope with these complex techniques except through continuous education?

You can, of course, learn much by your own experience -- but the School of Experience is one of the most expensive ways of securing a business education. The money that is lost daily in the trial-and-error classroom would stagger the imagination if it could be recorded and compared with other educational costs.

You can learn from the experience of others. But this too is time-consuming and haphazard.

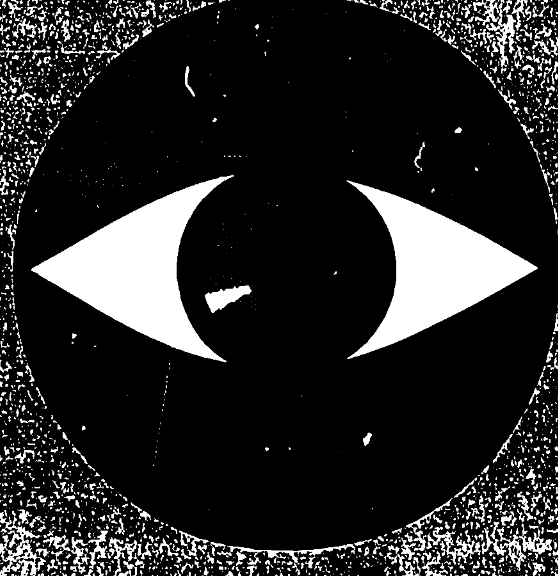
You can learn from your supplier, your trade association, and the other resource people who stand ready and available to share their business and professional know-how if you only go to them with willingness, openness, and confidence.

You can, perhaps, learn best by doing what you are now doing -- sitting down to a series of practical give-and-take conferences on the problems and potentials of effective management.

Your Distributive Education Service is a function of your local schools and your State Board of Education. The Small Business Administration is an agency of your Federal Government that has as its specific function the fostering and protection of small business. Together both agencies stand ready to help you.

Finally, one parting shot. Don't let the future come to you as an unwelcome guest. Don't let it be the past again, entered through another gate.

If you are receptive to new ideas and new techniques, if you agree that all you have learned in your lifetime has not been an education, but the beginning of an education, if in short, you believe with H. G. Wells that: "Human history becomes more and more a race between education and catastrophe," and if you act accordingly -- the future is yours -- wrap it up!



THE VISUAL AIDS

A What to Show

Section

[illegible]

USE OF VISUAL AIDS

WHAT TO USE	WHEN AND HOW TO USE

Chalkboard

Study and plan before a meeting what to put on the board and where to put it. Use it to present sketches, diagrams, outlines, definitions, key words, directions, record of class contributions, and summaries.
Suit material to board space.
Write plainly and quickly.
Keep wording simple.
Stand at one side of board while referring to material.
Talk to the group, not to the board.
Erase material no longer needed.

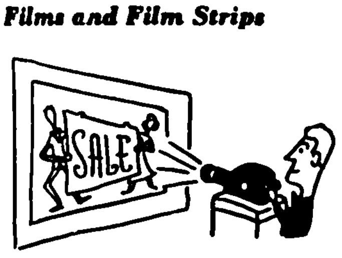
Posters, Charts, and Diagrams

To arouse interest and attract attention; to show relationships and trends; to inspire group.
Use device large enough to be seen.
Post where everyone can see.
Present at right time.
Discuss information illustrated.

Hand-Out Materials

To present information uniform in character and as a guide to material covered; emphasize key points; arouse interest and discussion; review or summarize discussions; and serve as permanent reference.
Select to serve a definite purpose.
Introduce at right time.
Distribute in manner to convey its importance.
Direct members how to use.

Films and Film Strips



Present an overall view; introduce a new subject; emphasize specific aspects of a subject; arouse interest; summarize.
Select carefully to relate to the discussion and plan presentation. Arrange room and equipment for showing. Alert the audience for the showing or what will be seen. Run the film. Discuss the subject matter and summarize.

Samples, Forms, and Exhibits

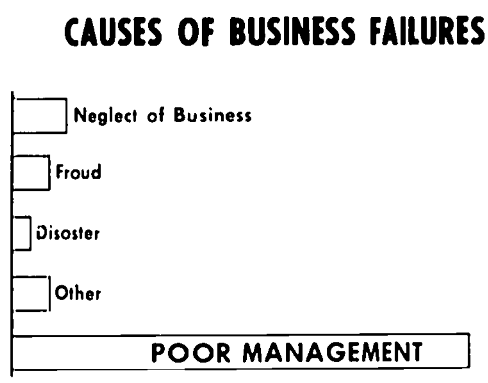
Keep subject matter practical; show development of a process; increase understanding.
Select only enough to illustrate, not confuse.
Pass around if necessary.
Take time to present clearly.
Comment when presenting.

Pedestal Chart

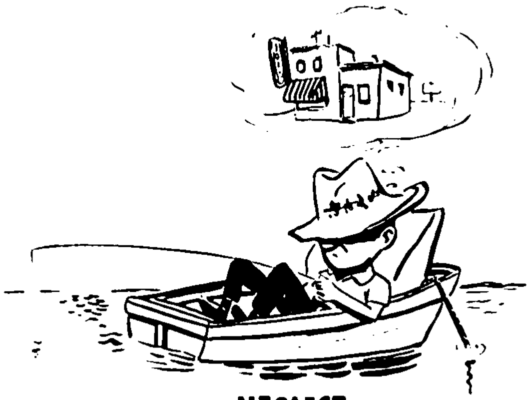
A pad of newsprint sheets or similar paper may be used for the same purposes as the chalkboard. Material recorded with chalk or crayon may be saved for future reference by the group or by the instructor.

732-928 O-64-5

OVERHEAD PROJECTUALS

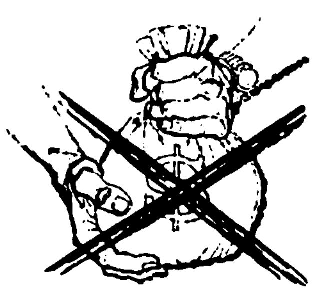


1



NEGLECT

2



FRAUD

3

DISASTER

4

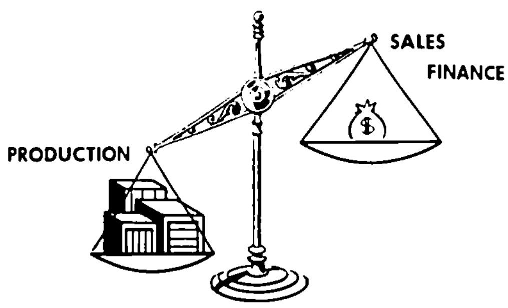
LACK OF
EXPERIENCE IN THE LINE

5

LACK OF
MANAGEMENT EXPERIENCE

6

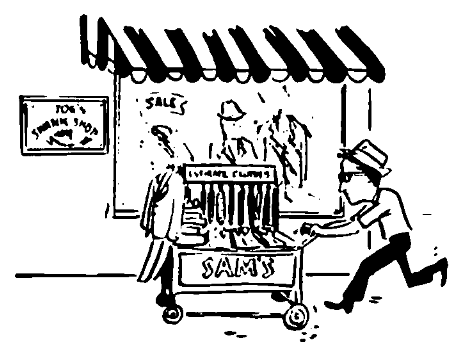
OVERHEAD PROJECTUALS



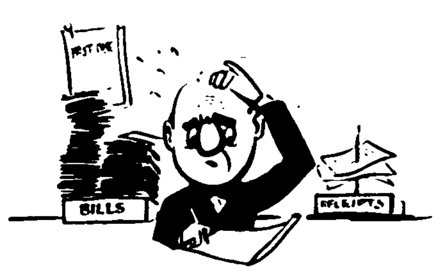
UNBALANCED EXPERIENCE

INCOMPETENCE

INADEQUATE SALES



COMPETITIVE WEAKNESS



POOR COLLECTIONS

TOP HEAVY EXPENSES

OVERHEAD PROJECTUALS

EXCESSIVE FIXED ASSETS

13

INVENTORY TROUBLE

14

POOR LOCATION

15

WHY BUSINESSES FAIL

Underlying Causes of Business Failure

Figures are rounded out since percentages vary little from year to year. If desired, current figures may be obtained from any Dun & Bradstreet, Inc. office.

Underlying Factors

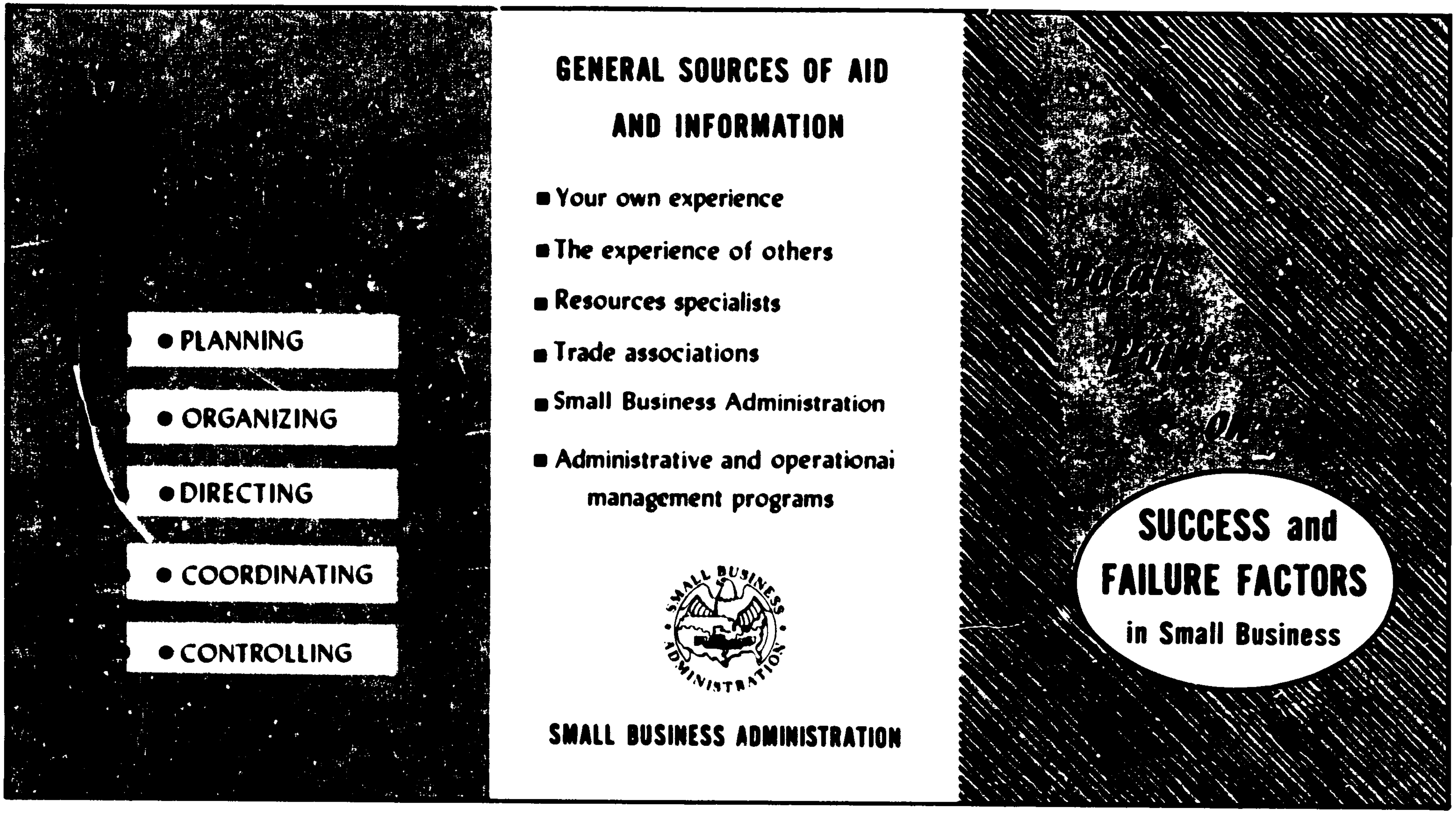
	3%	Neglect
	2%	Fraud
	1%	Disaster
	2%	Unknown
Total	8%	

Management Failures

	9%	Lack of experience in line
	18%	Lack of management experience
	20%	Unbalanced experience
	45%	Incompetence
Total	92%	

The above four management weaknesses resulted in failure through:

48%	Inadequate sales
9%	Top-heavy expenses
10%	Poor collections
8%	Inventory troubles
7%	Excessive fixed assets
3%	Location problems
21%	Competitive weakness
3%	Other



This page and the following illustrate a three-fold leaflet which summarizes the subject presentation. The leaflet is available in quantity from your regional Management Assistance Division Chief for distribution to participants in SBA-cosponsored administrative management courses.

SMALL BUSINESS STATISTICS

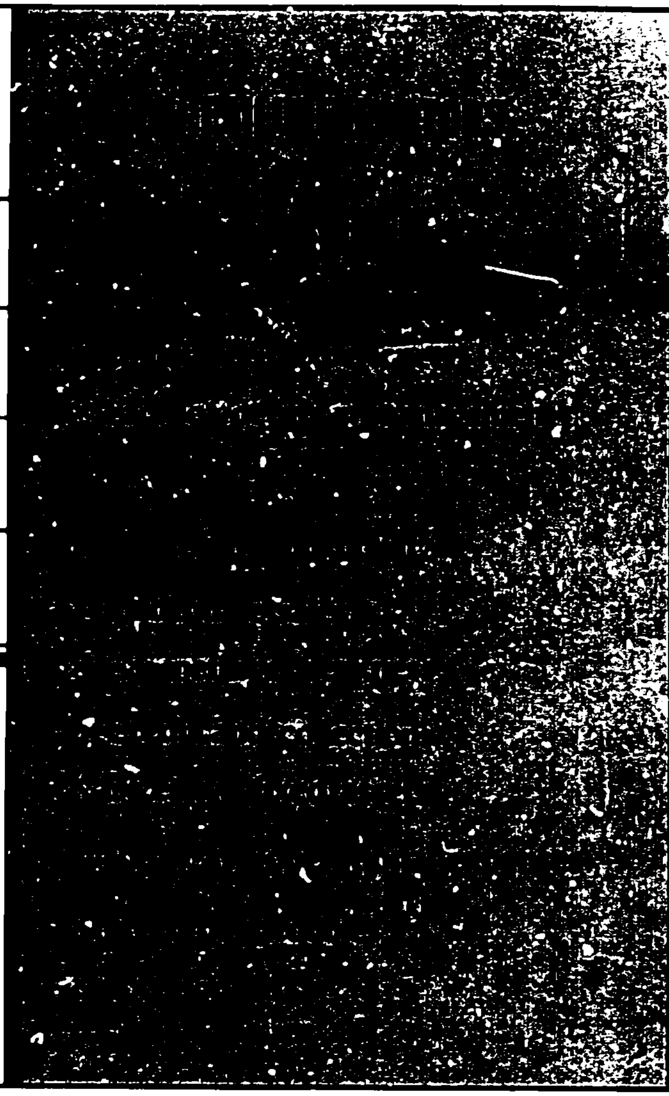
	of American businesses are small businesses
	of total business volume is done by small firms
	of our working force is employed in small concerns
	of small business failures are management failures

CHARACTERISTICS OF SMALL BUSINESS OPERATORS

Independence

Sense of enterprise

Personal involvements



√ PREREQUISTITES FOR BUSINESS SUCCESS

√ Existence of genuine business opportunity

√ Management ability and background

√ Adequate capital and credit

√ Modern methods

√ Insurance for measurable risks

√ A management philosophy

SMALL BUSINESS ADMINISTRATION

Management Research Summary

No. 9

Washington 25, D. C. January 1961

PROBLEMS OF SMALL RETAILERS

By *J. L. McKeever*, University of Wyoming, Laramie, Wyoming.

HIGHLIGHTS

The extension of credit, with slow payment by customers, was the financial problem most frequently mentioned by the businessmen cooperating in the study summarized here. A build-up of accounts receivable to the detriment of cash balances inevitably leads to a shortage of capital for the financing of other basic business functions.

Very few of the employers surveyed complained of high wages; most complaints concerning labor dealt with competence, initiative, attitudes, and productivity of employees.

Many employers do not recognize the fact that added costs resulting from high labor turnover are a major problem.

Financial ratio analysis is essential to the understanding of business operations. It reveals weak spots and provides a basis for remedial action.

Planning, forecasting, and control should not be looked upon as functions of large firms only. No matter what the kind or size of business, a prime requisite to success is the maintenance of proper sales, inventory and price ratios in relation to prevailing economic conditions.

The purpose of the project reported here in summary form was to determine and define the administrative and managerial problems faced by Wyoming's independent retailers. Personal interviews and mail questionnaires were used during the summer of 1959 to gather data from 487 businesses. The businesses may be classified as follows:

Type	Number	Percent
Service Stations	52	10.8
Liquor, Beer, Bars	39	8.0
Grocery Stores	52	10.8
Drug Stores	28	5.7
Restaurants, Cafes	56	11.6
Dry Goods, Department, Mercantile Stores	20	4.1
Candy, Confectionery, Retail Bakery Stores	11	2.2
Florists and Nurseries	14	2.8
Flour, Feed, Grain Fertilizer, etc.	10	2.0
Furniture, Appliance, Music Stores	45	9.3
Apparel Stores	41	8.8
Jewelry Stores	18	3.5
Hardware & Sports Stores	26	5.1
Variety Stores	9	1.8
New Car, Auto Accessories, Farm Equipment	66	13.5
Total	487	100.0

From the responses to the questionnaire used in the study, a pattern emerged that can be considered as defining the major problem areas of small retailers in Wyoming.

LABOR PROBLEMS

Of the 487 businesses studied, 439, or 90 percent hired employees either part time or full time. Two hundred and seventy-nine of the 439, or 64 percent, mentioned the procurement of competent, qualified employees as a major problem. Many felt that there was a general shortage of labor, but the problem was most acute where technical training or experience was needed for efficient performance on the job.

This seems to point to the conclusion that small business management faces the necessity of training its own employees. However, responses to questions regarding training practices indicated that very few training programs exist. In those that do exist, the

AVAILABILITY OF THE FULL REPORT

Copies of the full report, titled "A Study of the Problems of Small Retailers in Wyoming," may be obtained free upon request, from the Division of Business and Economic Research, College of Commerce and Industry, University of Wyoming, Box 3275, Laramie, Wyoming.

This report was prepared under a grant program of the Small Business Administration. It may be reviewed at any SBA field office or at certain depository libraries whose addresses may be obtained from the SBA field offices or from the Small Business Administration, Washington 25, D.C.

training is very informal and limited. There were a few instances where franchised dealers – such as those selling new cars and farm equipment – sent their mechanics and sales personnel to company schools.

Another problem mentioned frequently was that of keeping competent employees once they were hired and trained. Analysis of financial data relating to labor turnover indicates that the added costs resulting from high labor turnover are a major financial problem that is quite often not recognized by the employer.

Strangely enough, very few employers complained of high wages. Most complaints concerning labor dealt with competency, initiative, attitude, and productivity of employees.

COMPETITION

The various aspects of competition were considered major problems by a large number of retailers. Specifically, remarks centered about such competitive factors as (1) excessive number of businesses in one area, (2) chain store competition, (3) competitors offering special discounts to attract customers, and (4) price cutting. A large number indicated that their competitors had a better advertising program, were able to buy at lower prices, had stronger financial positions, had better locations, or were older, more established firms.

Some of the methods utilized to meet competition were price cutting, offering better service, provision of better parking facilities, offering better quality products, and extension of credit.

MERCHANDISING

As might be expected, these retail businesses considered the problem of merchandising one of their greatest challenges. How to increase customer traffic and, hence, sales volume was the major problem in this area.

The dilemma of advertising--to whom, where, when, and how--also posed difficulties, although in general, the retailers seemed to feel that advertising was an effective means for increasing sales volume. Two hundred and fifty-one respondents, or 52 percent, indicated that no attempt was made to measure the effectiveness of the various media.

To many retailers catering to the tourist trade, seasonal fluctuations presented another major merchandising problem. The seasonal aspect,in turn, created other business problems such as financing, and retention of qualified labor during the slack periods.

BUYING

The major buying problems were (1) lack of sources of supply, and (2) the where, what, and when problems.

A possible cause of the source-of-supply problem is the large land area and sparse population of Wyoming, as well as its distance from more heavily populated areas. These factors may combine to reduce the competition among suppliers to the disadvantage of Wyoming merchants. A possible, or at least partial, solution might be some type of merchants' cooperative. A possible solution to the problems of what to buy, and when and where to buy it, might be a more extensive and intensive analysis of markets by the retailer.

PLANNING AND FORECASTING

Two hundred and twenty merchants reported that they did not attempt to forecast sales, costs, or business conditions. Four hundred and twenty six or 87 percent, indicated that they did not budget cash outlays and income, nor make any attempt to budget other expenditures.

Two hundred and thirty-four merchants said they had never determined the amount of sales needed to cover total costs and expenses of doing business. In other words, almost 50 percent of the businesses cooperating in this study had no concept of their breakeven point, a factor so crucial in proper planning and control of expenditures.

Planning, forecasting, and control are often looked upon as functions only of large manufacturers and not applicable to retail units. Actually, no matter what the kind or size of business, a prime requisite to success is the maintenance of proper sales, inventory, and price ratios in relation to prevailing economic conditions. At the present time, many businesses are succeeding because of the prevailing favorable economic conditions. The question the retailer must constantly answer is, "Could I survive a recessionary period or a major readjustment of prices?"

FINANCIAL PROBLEMS

Financial aspects of the business posed a major problem to the Wyoming businessmen. *The extension of credit* with slow payment by customers was the financial problem most frequently mentioned. Extension of credit was practiced widely – 346 businesses extended credit to all customers and only 64 did not extend credit at all. (Seventy-seven businesses--restaurants, bars, and concerns of a similar nature--extended credit on a selective basis.)

Another major financial problem was *lack of working capital.* This, of course, has a direct relationship to the problems of credit extension and slow payment. A build-up of accounts receivable to the detriment of cash balances inevitably leads to a shortage of capital to finance other basic and necessary business functions. Two hundred and eight businesses--43 percent--indicated either that they did not have sufficient cash with which to pay weekly expenses and suppliers, or that they were occasionally pinched.

Lack of financial analysis is known to be a rather common problem among small business managemen throughout the nation. It is also a problem for the small businesses taking part in this study. For example, 294 businessmen indicated that they were not familiar with financial ratio analysis, and another 40 stated that they had some knowledge of such ratios but did not use them in their businesses. One hundred and fifty-three said that they were familiar with and did use financial ratios in analyzing operations of their businesses. The use of financial ratios by this latter group, however, was generally limited to a net sales-cost-profit relationship and omitted many ratios necessary to good analysis.

Three hundred and sixty-seven, or 75 percent, of the cooperating retailers felt that a better financial analysis of their business could be made. Responses to another question revealed, however, that 224 businessmen, or 46 percent of the total, did not have the education or experience necessary to make a rational analysis of their financial statements.

FINANCIAL RATIO ANALYSIS

Financial ratio analysis is not a panacea, but it is essential to the understanding of operations. It reveals weak spots and provides a basic for remedial action.

A considerable amount of financial data was requested from the firms included in the survey. In turn, each participant was promised a financial analysis of his own firm and a comparison of his business ratios with those of the group cooperating in the study and with the national averages. Seventeen ratios were computed for each firm and the averages for each classification (shoe stores, hardware stores, drug stores, etc.) were computed.

Of the 17, five key ratios are shown in the accompanying table. The five, chosen because they are frequently used in financial ratio analysis, are explained below.

- **Inventory Turnover Based on Cost of Goods Sold.** This ratio was computed by dividing the annual cost of goods sold by the average inventory at cost. The result indicates the number of times the retailer turns the dollar volume of his stock annually. The ratio is subject to some criticism because so many retail businesses make a physical inventory only during the last week in December. The ratio would be more meaningful if the retailer inventoried monthly and computed a 12-month average inventory.

Among the Wyoming retailers studied, inventory turnover was less in 17 of the business classifications than the national average for those classifications. This probably indicates that attention should be given to improving methods of inventory control and to increasing sales in order to make the Wyoming ratios more favorable.

- **Average Collection Period.** Two computations are necessary to arrive at an average collection period in days. The first is to divide the total annual credit sales by 365 days. (Credit sales are

SELECTED FINANCIAL RATIOS OF RETAILER GROUPS[1]

	Inventory Turnover on Cost of Goods Sold		Average Collection Period (Days)		Current Ratio		Cost of Goods Sold to Net Sales (Percent)		Total Expense to Net Sales (Percent)	
	Wyoming	National	Wyoming	National[2]	Wyoming	National	Wyoming	National	Wyoming	National
Service Stations	23.8	21.3	37		7.1	[2]	74	77	17	22
New Car Dealers	5.4	8.!	136		3.4	1.9	84	86	13	13
Auto Accessory	5.5	5.2	112		3.5	1.7	60	67	26	30
Farm Equipment	3.7	3.7	70		2.9	2.2	79	81	15	16
Furniture Stores	3.1	3.1	167		7.3	2.7	69	66	23	32
Household Appliances, Radio, Music	3.4	4.4	135		5.8	2.0	67	73	26	26
Shoe Stores	1.6	2.1	88		5.0	2.5	65	64	20	[2]
General Clothing	1.7	2.9	--		13.9	2.6	67	66	23	32
Ladies Wear	3.7	4.3	81		6.3	2.5	66	64	21	34
Mens Wear	1.5	2.3	156		8.1	2.4	66	63	24	34
General and Mercantile Stores	7.6	3.5	58		15.9	2.6	76	70	17	27
Dry Goods, Department Stores	2.4	3.5	--		11.9	2.9	75	67	23	31
Jewelry Stores	1.3	1.3	235		5.7	2.3	51	57	29	41
Variety Stores	1.9	2.9	124		18.5	[2]	63	61	30	36
Candy, Confectioneries, Retail Bakeries	9.7	11.8	59		6.5	[2]	54	64	26	35
Florists, Nurseries	5.6	7.4	31		4.3	1.4	44	57	41	41
Flour, Feed, Seed	7.6	6.9	86		3.2	3.1	79	79	18	19
Wine, Liquor, Beer	8.0	8.2	--		11.7	1.7	61	83	26	14
Groceries	15.1	19.1	59		9.2	1.5	83	84	11	15
Drugs	3.4	4.3	90		7.2	2.5	66	71	21	27
Restaurants, Drive-ins	51.5	22.4	19		3.6	.9	49	47	42	50
Hardware	2.5	2.8	99		6.7	2.9	67	71	25	26
Sporting Goods	5.0	3.1	319		7.9	2.5	78	73	18	25

1/ National-average figures are taken from published information contained in Statement Studies (Robert Morris Associates) and Operating Ratios for Forty-one Lines of Retail Trade (Dun and Bradstreet).

2/ Not available

account sales exclusive of installment sales.) The resulting figure represents average daily credit sales. The second computation is to divide the outstanding accounts receivable at the end of the accounting period by the average daily credit sales determined in the first computation. The resulting figure represents the number of days of credit sales in accounts receivable.

The unusually high average collection period found in several of the retail classifications may be due to one or both of the following reasons:

1. A substantial number of account sales are made during the last few weeks of the accounting period, i.e., during the Christmas season.
2. Collections of accounts receivable are very slow.

If the assumption is made that most firms extend 30-day credit, the data indicate that practically all the retailer groups have permitted control of accounts to get out of hand.

- **Current Ratio.** The current ratio is computed by dividing current assets by current liabilities. The resulting ratio is usually expressed as the relation of dollars of current assets to one dollar of current liabilities; i.e., the first current ratio in the table, 7.1, should be read as $7.10 of current assets for each $1 of current liabilities.

The data shown here on current ratios indicate a generally favorable pattern among the firms in the survey.

- **Cost of Goods Sold to Net Sales.** The cost of goods sold includes the purchase price of inventory plus freight and less discounts. The ratio is determined by dividing this cost by net sales. The resulting figure is the percentage of the net-sales dollar devoted to costs of goods. The difference between the cost-of-goods-sold percentage figure and 100 percent represents the percent of the sales dollar available for operating costs and profits.

For the Wyoming retailers surveyed the cost-of-goods-sold percentages as shown in the table are almost equally divided as to favorable or unfavorable when compared to national percentages.

- **Total Operating Expense to Net Sales.** This computation is made by dividing total operating expenses by net sales. The resulting figure is usually expressed as a percentage. The figure when subtracted from the gross profit percentage represents the net profit in percent, before income taxes, owner's salaries, and other income and expenses. For control purposes, the ratio is an excellent one to indicate trends in operating expenses.

The percentages for the Wyoming firms compare very favorably with the national averages. It appears, therefore, that operating expenses among Wyoming firms included in the survey are generally less than for the nation as a whole. Since labor normally represents a substantial part of operating expenses, further analysis would probably reveal that the lower operating costs of the firms surveyed result from lower labor cost.

Washington, D.C., March 1962

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency
JOHN E. HORNE, Administrator

Management Research Summary

Small Business Success and Failure Cases

Prepared for the State of Oklahoma Department of Commerce and Industry
By *N. H. Ringstrom*,* Professor and Head, Department of Marketing
Oklahoma State University, Stillwater, Oklahoma

HIGHLIGHTS

Studies of contracting firms in the construction industry and of home furniture and appliance retailers brought out these points:

The successful contractor (1) prepares detailed cost estimates before submitting a bid; (2) knows his capabilities and those of his firm and operates within them; (3) keeps close track of his costs on each contract and the relation of these costs to those budgeted in the original estimate and bid; (4) recognizes his limitations and seeks professional help when he needs it.

The successful home furniture and appliance dealer (1) starts his firm only when it can be properly and adequately financed; (2) is careful in granting credit; (3) gives careful attention to the selection, training, and supervision of his employees; (4) understands all phases of merchandising.

Some business firms succeed and others fail in the same types of business activity and under similar circumstances of time and area of operations. Why? Can the reasons for success or failure be discovered?

The study summarized here undertakes to establish some markers on the roads to business success or failure for two types of small business--contractors in the construction industry and home furniture and appliance retailers. These markers were determined on the basis of personal interviews with businessmen, bankers, lawyers, accountants, and others whose experience qualified them to express informed and unbiased judgments on the success or failure of the business firms under study.

CONSTRUCTION INDUSTRY CONTRACTORS

Most contractors in the construction industry are small businessmen. Some large firms operate in this field, but usually major construction tasks are accomplished by assembling through subcontracting the resources of a number of small firms. The conclusions that follow are based on a study of a number of such contracting firms in Oklahoma.

AVAILABILITY OF THE FULL REPORT

Copies of the full report, titled "Case Studies in Business Success and Failure," may be purchased for $2.50 from the College of Business, Oklahoma State University, Stillwater, Oklahoma. Make checks payable to College of Business, Oklahoma State University.

This report was prepared under the 1959 Small Business Management Research Grant Program of SBA. It may be reviewed at any SBA field office or at certain depository libraries whose addresses may be obtained from the SBA field offices or from the Small Business Administration, Washington 25, D.C.

*Project Supervisor; other members of the research group are listed on page 4 under "About the Study."

• <u>The successful contractor carefully prepares detailed cost estimates before submitting a bid.</u>

Among the firms studied, without exception the successful contractors literally "built the job on paper" before arriving at a bid figure. Preparing a bid properly requires time, effort, and attention to detail. Bidding, regardless of the size of the job, is extremely competitive.

The procedures involved in producing the accurate, detailed cost estimates needed in the preparation of a sound bid are fairly simple and are well known in the industry. Yet, in virtually every case of failure analyzed in this study, the difference between profit and loss, or between success and failure, could be traced to the use of substandard bidding practices and the submission of bids that were fundamentally unsound and unprofitable.

• <u>The successful contractor knows his capabilities and those of his firm, and operates within them.</u>

Overexpansion can be a problem to the small contractor. First, the loss resulting from only one significant mistake on a large contract can wipe out the existing equity of a small contracting firm.

Second, losses resulting from several simultaneous contracts, even when they are not large individually, may be sufficiently damaging collectively to put a small firm out of business.

All the successful contractors, on the other hand, recognized the necessity of following each job very closely. They also recognized the need for experienced, high-quality supervisory assistance. The successful contractors did not accept more work than they and their supervisory staffs could handle adequately.

• <u>The successful contractor keeps close track of his costs and the relation of these costs to those budgeted in the original estimate and bid.</u>

The successful firms in the study carefully allocated expenses to particular jobs and made sure that each cost was clearly identified. Every item of expense was traced to its proper destination. Furthermore, all the successful contractors made systematic use of this information. A comparison of actual costs and cost estimates in the bid enabled the successful managers to detect trouble spots immediately and to take appropriate action.

The unsuccessful firms showed a very different pattern in this respect. In some of the failures studied, effective recordkeeping was practically nonexistent. In others, records were kept very carefully, but the information was not transmitted to, or used by, the management.

• <u>The successful contractor recognizes his limitations and seeks professional advice when he needs it.</u>

Observations of interviewed, successful as well as unsuccessful contractors suggest that many contractors with good technical backgrounds developed on the job, lack business or management experience. Bankers, lawyers, accountants, bonding-company representatives and others pointed out that some of the major difficulties of unsuccessful contractors are due to failure to recognize the need for outside professional or technical assistance. This is especially true of the beginning contractor who is trying to expand his operations in a hurry.

The use of professional advice is particularly important in connection with contracts. Failure to understand the legal consequences of clauses inserted by customers may be a source of serious loss to a contractor.

HOME FURNITURE AND APPLIANCE RETAILERS

The home furniture and appliance field is fairly typical of retailing generally. Cases of bankruptcies are concentrated heavily among relatively young firms with major shortcomings. The typical owner-operator succeeds in making a living, though he does not accumulate great wealth. He takes pride in his independence, which he pays for with long working hours and the many problems he could avoid by working for a firm other than his own.

• <u>The successful dealer starts his firm only when it can be properly and adequately financed.</u>

The study revealed that the unsuccessful home appliance and furniture dealers had started their operations with insufficient capital. This lack of initial funds continued to hamper operations throughout the life of the firm.

The nature of the home furniture and appliance field is such that a large, well-assorted inventory is very costly. Many of the items handled are expensive. The financially weak dealer must find assistance outside his own firm in order to maintain even a comparatively small inventory.

It was found that the unsuccessful dealers, in attempts to increase sales volume through increased inventories, went heavily into debt to suppliers. At times, the suppliers owned every item in stock, including those on the sales floor. (Floor-plan renewals carry a high financing rate.)

The successful dealer, on the other hand, starts his firm only when he can make an initial cash purchase of an adequate inventory of merchandise for display and sale. His inventory may not be large; but at least he can, in most cases, meet the requirements of his customers. He continues to make cash purchases of merchandise in the operation of his firm. Thus he is in a financial position to take advantage of all discounts from suppliers.

Successful retailers in this field take cash discounts and other discounts from suppliers at every opportunity. Owners in the cases studied reported that this practice resulted in major contributions to profits.

Financing of customer accounts is another area in which inadequate capital contributes to failure of the firm. Many major appliances and items of furniture are purchased by retail customers through installment credit. The dealer who is not financially able to grant this credit on his own must make other arrangements. Typically, he sells his accounts receivable at a discount to banks and finance companies. Such arrangements are easily made, but the cost to the firm is high.

In contrast to this practice, the successful dealers interviewed all agreed on the desirability of financing their own customers. This requires considerable financial strength, but the profit potential is high. The interest and other financing charges paid by the customer over a period of perhaps 18 to 24 months were found in a number of the cases analyzed to equal or exceed the dealer profit realized on the item of merchandise sold.

These firms reported that they found a further advantage of self-financing in the continuing relation with credit customers. A significant number of "add on" and repeat sales result from this prolonged contact.

• The successful dealer is careful in granting credit. He investigates each prospective account thoroughly. Customer credit is looked upon as a privilege, not a right.

Many of the dealers who did not survive had granted credit indiscriminately in their efforts to build sales. Bad accounts and repossessions had led to losses for virtually every one of the failure firms analyzed in this study.

Credit sales may be financed by agencies outside the firm, but bad accounts ultimately result in deductions from the "reserves" required by the financing agencies. In some cases, retailers are forced to buy back from financing agencies accounts that have proved uncollectible.

If there is enough collateral, loans may be secured from banks to supplement inadequate operating capital. However, many of the bankers interviewed in connection with the study expressed reluctance to make loans to firms with poor credit management. Also, borrowing money for this purpose is expensive. When loans become excessively large, the interest charges are a serious drain on the company's operation.

• The successful retailer of appliances and home furnishings gives careful attention to the selection, training, and supervision of his employees.

Personnel costs in retailing typically constitute the largest expense item on the operating statement. The successful dealers interviewed were aware of this fact and made every effort to realize the best possible returns from this investment.

The firms that had failed either did not understand the importance of this factor or did not know what to do about it. Selection of personnel was haphazard. Little training was offered. Turnover was high.

Supervision in the unsuccessful firms, too, was inadequate. The owner-manager usually dealt with the more obvious problems as they came up, but he failed to check systematically on the performance of his employees. All the less successful dealers in the study lacked experience and training in the organization and management of people.

• The successful home furniture and appliance dealer understands, not just selling, but all phases of a merchandising operation.

In addition to areas already discussed, the successful dealer in home furniture and appliances is skilled in (1) proper use of advertising and other types of sales promotion; (2) selection of merchandise his customers like; (3) the pricing of this merchandise, not only at profitable levels, but also at figures customers are willing to pay; (4) provision of good customer service, especially repair service; (5) proper selection of store location and good use of store layout; and (6) the institution and use of internal controls, including cost accounting.

The successful owner-manager works hard, uses good judgment in selecting key people, and depends on other qualified individuals to accomplish specialized functions.

ABOUT THE STUDY

The conclusions reported in this summary are based on a detailed investigation of more than 40 firms, including both successful and unsuccessful firms. Interviews were held, not only with members of the firms under study, but with credit-rating organizations, bankers, suppliers, competitors, customers, and others who had had business contacts with the cooperating firms.

To qualify as a "failure" case, a firm had to be formally declared bankrupt between January 1, 1954, and January 1, 1959. To qualify as a "success" case, a firm had to be at least 5 years old and had to be considered successful by those who knew enough about it to judge objectively.

Successful firms were matched as far as possible with unsuccessful ones as to time covered, business environment, size, background, line of business, and type of operation.

The full report includes detailed case studies of 11 of the firms studied.

The following members of the staff of Oklahoma State University were associated with Dr. Ringstrom in the study: E. B. Austin, Associate Professor of Accounting; J. L. Garner, Assistant Professor of Office Administration; D. L. James, Instructor in Marketing; F. J. McDonald, Assistant Professor of Business Law; R. T. Morgan, Assistant Professor of Business Law; C. Roman, Professor and Head, Department of Management; R. W. Trenton, Professor of Economics; J. S. Wagle, Professor and Head, Department of General Business; P. A. Weinstein, Instructor in Economics.

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SMALL BUSINESS ADMINISTRATION
U. S. Government Agency
JOHN E. HORNE, Administrator

Management Research Summary

SMALL BUSINESS PROBLEM STUDIES

By *John B. Kline* and *John T. Doutt*, Bureau of Business Research
University of Colorado, Boulder, Colorado

ABOUT THE STUDY

The research reported in this Summary consists of case studies of small manufacturing companies and small retail, wholesale and service establishments in the Rocky Mountain area. The cases were selected to represent a cross-section of the small business community in that area.

Each case is presented in a narrative style and depicts a particular problem or problems confronting the owner-manager or management group. The narratives in many cases are documented by various exhibits which support the situation: for example, organization charts, cost schedules, sales records and charts, personnel schedules, maps, job descriptions, balance sheets and income statements, inventory records.

Material for the case studies was obtained by depth interviews with the top managers of each firm studied.

The 26 cases which make up the research described in the following pages represent a systematic effort to collect examples of small business operations in the Rocky Mountain area over a broad range of activity. The full study is divided into two major areas, the first dealing with manufacturing enterprises, and the second with retailing, wholesaling, and service establishments.

The cases are designed primarily for educational purposes and are deemed to have sufficient detail and dimension to lend themselves to analysis and a statement of recommendations. At the same time, they often illustrate a problem situation and an acceptable solution as experienced by a small businessman in a specific business. The preface of the full report states that they will be of value to those concerned with teaching small business subjects as well as those whose livelihood depends on the successful operation of a small business enterprise.

In the management area, special effort was made to approach each case from a policy level. Many companies interviewed thought they had specific problems that ought to be worked out immediately. In one situation, concern with the existing organizational arrangements was expressed. But analysis of the company suggested that a far more basic problem had to do with company objectives and future goals.

The management group in still another case was concerned over the profitability of its warehouse operations. However, interviews revealed that a power struggle within the management group was in progress. The

AVAILABILITY OF THE FULL REPORT

Copies of the full report, titled "Case Problems of Small Business in the Rocky Mountain West," may be purchased for $2.50 from the Bureau of Business Research, University of Colorado, Boulder, Colorado. Make checks payable to the Bureau of Business Research.

This report was prepared under the 1959 Small Business Management Research Grant Program of SBA. It may be reviewed at any SBA field office or at certain depository libraries whose addresses may be obtained from the SBA field offices or from the Small Business Administration, Washington, D.C.

basic problem was that the absentee owner had failed to indicate proper business objectives and appropriate methods for assuring their attainment.

If it is the function of top management to set proper goals and assure their attainment, the report points out, it is no less the function of middle management to be concerned with effective solutions of day-to-day problems. Therefore, some of the cases, particularly those in retailing, wholesaling, and service fields, were selected to point out the problems of the small businessman who, as the top-level decision maker in his operation, finds himself carrying out his ideas and implementing his goals with little or no aid except for a clerk or occasional advice from his accountant. In these cases, typical of many small businesses, the line between top and middle management is not clearly drawn or does not seem to exist at all.

SMALL BUSINESSMAN PROFILE

In the preface to the full report, the authors present what they describe as a profile of the "typical small businessman in the Rocky Mountain area," based on their case studies. Typically, he is middle-aged and has been engaged in some type of small business most of his working life. In many instances, he was associated with some small business during the depression years of the 1930's. He has established his business by capitalizing on an economic need for his particular services or products as well as by adjusting ingeniously, if not always logically, to his environment.

• Outside Information Sources. This "typical" small businessman belongs to the Chamber of Commerce but, as a rule, he does not work very actively in its programs. He reads some business and trade publications but makes limited use of information and data which require alteration or interpretation for his own use. He is constantly searching for specific answers to his particular problems, which are often his personal attitudes.

• Attitudes. The general attitude of the "typical" small business executive is that of continual apprehension toward persons and forces he views as a threat to his position. He may feel that some conditions imposed by legislation or by the size of his operation are the most serious and objectionable features of his business. Quite often, these are not things a consultant or advisor would deem paramount but, because of the personality of the individual, they assume unwarranted proportions. He is conservative in his viewpoint and resists political and economic changes as bringing about conditions requiring adjustment that he is reluctant to tackle.

This "typical" small businessman can also be described as a persistent and tenacious "free enterpriser." He tends to view his job as one where he must struggle constantly to resist the narrowing aspects of Government regulation, the fickleness of the customer, and the seemingly unwarranted demands of his employees. He may tend to regard human relations skills as ineffective and unrealistic.

His attitudes are shared by his customers and by his business colleagues, so that he is not imposing on them conditions which are unknown or unexpected. His employees accept readily his direct approach and consider that they too may someday run their own businesses with a firm hand. Viewed by his business associates, he is friendly, considerate, and willing to go out of his way to help his customers and even his competitors on occasion

Based on these observations, the "typical" small businessman in the Rocky Mountain area who can adjust socially and economically to the community in which he operates should be able to do well.

PATTERN OF CONDUCT

The authors also point out that the following four points were observed frequently enough in the case studies to warrant them as generalizations about the pattern of conduct of small business executives in the Rocky Mountain area:

1. Considerable skepticism is evident in the minds of many of these businessmen regarding academic knowledge and training. They are also unwilling to accept advice and counsel from educators to the extent that the executives of large business do.
2. Many business problems are met in a "head-on" fashion without careful consideration being given to the long-range effects. Hiring, firing, disciplinary action, product increase, retaliatory action all are a part of the day-to-day job of the small entrepreneur.
3. There is a definite lack of long-range planning. Many managers get around to making policy or administrative decisions only under conditions of duress or by default. Decisions of this type are avoided until dire necessity requires action.
4. Little training and consultation are devoted to the average employee. Frequently,

employees are left without much idea as to their responsibilities and who their supervisors and/or subordinates are. The manager may occasionally take issue with an employee, assume or reject jurisdiction over a given matter, or perhaps reprimand an employee rather severely. These are probably thought desirable and certainly justified as a management prerogative.

Two conclusions are drawn from these generalizations: (a) Many conditions of the past on which ambitious businessmen built an empire have been squeezed farther and farther from the industrial and commercial complexes that characterize the American scene. (b) The area where these features are still dominant is the small business--particularly, such businesses as might be found in the Rocky Mountain area.

RESUME OF CASE STUDIES

A manufacturer of women's specialty wear. In this case, a small manufacturer was attempting to obtain national distribution. Problems of sales management and of production control are presented in a detailed and comprehensive fashion.

A manufacturer of specialized sporting equipment. Here, a small manufacturer describes something of the marketing characteristics of his niche in a large industry. Problems of organization and production characteristic of many small businesses are presented. The case closes with an interesting statement by the managing partner as to his philosophy regarding small business and its place in our economy.

A small, franchised implement dealer located in a rural area. In this case, the owner describes some of the difficulties of survival in the farm implement business. The case presents a sharp picture of how the changing farm situation is affecting the small implement dealer. Numerous financial statistics are presented which trace in specific fashion the dealer's declining profit margin.

A small manufacturer grows and then diversifies. In this case, a small manufacturer who made his name and fortune on a rather narrow product line finds himself in a financial position that will enable him to diversify. The case traces the various avenues he pursues in his attempt at product diversification.

A "penny stock" uranium company. In this case, a man combines an idea and limitless energy to make a spectacular success story. Beginning as a speculative venture, the enterprise develops into a profitable and stable business organization.

A partnership manufacturing safety equipment and metal tools. This case illustrates the ups and downs of a business originally based on a narrow product line.

A steel fabricating firm specializing in construction equipment and parts and concrete batching equipment. In this case, nonowner management tells of its day-to-day operating problems and the difficulties of establishing long-range goals for the company. It finds its areas of authority clouded and its responsibilities varying and uncertain.

A concern specializing in fabricated steel parts in which engineering plays an important part. In this case, the owner-operator tells how he intends to find a market niche by specializing in the selling of his engineering talent, rather than a simple line of steel fabricated parts.

A small one-man business engaged in the cutting, polishing, and mounting of semi-precious stones into jewelry. This case describes a business which, conducted as it is, has reached its maximum growth.

A small town furniture store dealing in a complete line of furniture, floor coverings, and appliances. One of the problems of this retail establishment is caused by its unique premises--a main store, an annex, and a warehouse.

A rootbeer drive-in located at the edge of a small but good business town. This case illustrates the operations of 6-months-a-year business and the factors which are particularly important for its success.

A liquified petroleum gas sales and service organization serving two communities separated by about 45 miles. The problem of the owners of this business is the possibility of a cheaper substitute for its product.

A small, hardware business in a farming area where much row-crop farming is done. The business has stiff competition from chain operations, but tends to do well in fringe items, particularly shopping and gift items bought by women.

A chain of family furniture stores engaged in full-line selling. The business in this case has problems of organization, expansion, and stock control because of growth and desire to become bigger.

A small specialty packer who processes tomatoes into canned tomatoes, ketchup and puree. This case describes the operations of a competent operator who has competitive advantages on which he capitalizes.

A small, recently established manufacturer of pickup coaches and trailers. The problem facing the owners of the company in this case study is whether they should expand and, if so, in what direction and by what method.

A small savings and loan organization which has shown a rapid and substantial growth. This case is a good example of the type of organization that small businessmen might form to aid their own needs for property loans.

A laundry and dry-cleaning establishment which covers a wide territory and develops business by knocking on doors. This case illustrates the success of an aggressive but accommodating individual despite geographical disadvantages.

A tire-sales, service and recapping operation operating under a franchised arrangement. The policy of the absentee owner in this case is to enable his salaried manager to take over the ownership of the business eventually.

A small-town restaurant catering to high school, college, local population, and tourist trade. This case illustrates the need for the owner-manager's personal attention to all facets of his business.

An automotive tool manufacturer. This successful corporation has initiated an employee profit-sharing plan.

A retail lumber yard. The success of this firm is due to: (1) high volume of sales achieved per employee; (2) efficient utilization of its space and buildings.

A manufacturer of specialty fertilizer. Production problems and inability to meet competitive terms caused the company in this case to cease operation.

An equipment company dealing in materials-handling items. Marketing is the problem of the company in this case. The business has become very competitive; sales quotas of manufacturers are increasingly difficult to meet; customer trade-in and service costs are creating a profit squeeze.

An independent drugstore in a shopping area in a rapidly expanding community. The owner is faced with making two decisions: (1) how to meet newly established competition; (2) whether to expand his premises and, if so, in what fashion.

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SMALL BUSINESS ADMINISTRATION
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Management Research Summary

SMALL BUSINESS INSTABILITY AND FAILURE

By *Paul W. Paustian*, Professor of Economics, and *John E. Lewis, Jr.*, Research Associate
The University of Alabama, University, Alabama

HIGHLIGHTS

General economic conditions, personality problems, and poor judgment in starting the firm were the reasons found for about half the business failures studied.

The likelihood of failure was greater in industrial groups where a large proportion of the firms are small than in industry groups with a large proportion of big firms.

Some of the business failures could have been prevented only by not starting the business. More opportunity for professional counseling is needed by prospective as well as active small business operators.

The report summarized here takes issue with the conclusion reached by many studies of business failure that poor management is the primary cause in 9 out of 10 failures. Findings of the study on which the report is based indicate that this was not true of the Alabama firms studied unless the term "management" is used very broadly. General economic conditions, personality problems, and poor judgment in starting the firm accounted for about half the failures.

Management problems undoubtedly do exist in most failure cases. But the causes of failure in about one-third of the firms studied had deep roots in social and economic conditions outside the business.

One firm, for example--a farm-equipment dealer--was located in a county where row crops were rapidly giving way to timber and cattle. New and fewer types of machinery were required. Furthermore, the county had been losing population by out-migration. The market for all goods was declining.

Some of the firms were never serious contenders for inclusion in the ranks of established businesses. Some started without enough capital to ride out even the first few difficult months that almost any new firm must face. Others were purchased as semi-going concerns and failed because of absolute lack of demand for the type of goods or service they offered.

These and other cases of poor preoperative judgment made up a large part of the first-year failures. This can lead to overstatement of the seriousness of poor management in small firms--which, the report comments, does not need overstating.

PATTERNS OF INSTABILITY

A statistical study was made of instability among all Alabama firms from 1939

AVAILABILITY OF THE FULL REPORT

Copies of the full report, titled "Small Business Instability and Failure in Alabama," may be purchased for $1.00 from the Bureau of Business Research, P.O. Box KK, University, Alabama.

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to 1960. The likelihood of failure was found to be greater in industry groups where a large proportion of the firms are small than in industry groups with a large proportion of big firms (see table). The lowest rates of instability were found in counties where there had been little industrial development.

- Mining Firms

The two industries showing the greatest instability over the 21-year period were sawmills and mines. Mechanization of larger mines and the substitution of other fuels for coal help to explain the reduction in the number of mining firms.

Also, in many parts of Alabama, miners released by the large, modern mines supplying the power and steel industries may be out of work for some time. When this happens, the number of "wagon mines," as they are called in the trade, increases.

The workers, however, turn to urban industrial jobs when possible. Thus, the business cycle contributes to the instability of the mining industry.

- Sawmills

Sawmills in Alabama have been, in terms of numbers, primarily of the portable variety in recent years. Hardwood in the State was largely cut over in the twenties, and opportunities for profitable large-scale operations have diminished since that time.

About three-fourths of the sawmill operations in the State at the present time are portable mills operated as seasonal activities by farmers. The statement of a South Alabama farmer currently out of the sawmill business is typical of most sawmill operators in the State.

"My mill's out in the shed," he said. "If prices get better or I get a little spare time, I may set up again. There are 5 or 6 mills within 10 miles of here in the same condition. If the lumber business picks up a little, most of them will probably go back in the business."

It is apparent that the rates of instability in the coal mining and sawmill busi- sses are not represen.ative of business cl. re in the popular sense. Many sawmills and small coa.. mines are simply dormant. They are waiting for economic conditions in those or other industries to shift to the point where their operations will again be profitable.

There are other exits--a wide range of them--between economic failure and selling out at a profit. Only by investigation of the individual firm is it possible to know through which exit a firm has left the arena.

SOME CASE STUDIES

In order to study aspects of business failure that do not come to light in reports covering only financial factors, a number of individual nonbankrupt business failures were examined. For the purposes of this part of the study, business failure was defined as the disposal of a business to avoid financial loss.

The following outline lists the primary causes (shown with asterisk) and other contributing factors found in the failures of the firms studied. (names have been changed to avoid identification.)

Doss Manufacturing Company

*Conditions beyond control of the operator
Too rapid expansion, resulting in low cash position
Failure of operator to keep his head in a crisis

Lee Service Station

*Personality of the owner
Short-run profit maximization

Jones Farm Equipment

*Economic conditions beyond the control of the operator
Declining role of the business to which most of the sales were made
Inability to adapt to changing conditions

Short Sawmill

*End of short-run economic advantage
"Hibernation" rather than failure

Ray Service Station

*Laziness of operator

Business Instability in Alabama by Industry Group, 1939 to June 1960

Industry Group	Total Firms in Business* 1939 to 1960	Firms in Business June 1960	Total Firms Discontinued 1939 to 1960	
			Number	Percent
Agriculture	272	185	87	32
Mining	644	339	305	47
Construction	5,247	3,137	2,110	40
Manufacturing less sawmills	2,997	2,069	928	31
Sawmills	3,025	1,527	1,498	50
Transportation, communications, and utilities	1,340	943	397	30
Wholesale trade	3,264	2,547	717	22
Retail trade	11,990	7,568	4,422	37
Finance, insurance, and real estate	1,927	1,417	510	26
Service trades	3,631	2,382	1,249	34
Professional services	1,408	1,027	381	27
Unclassified	10	3	7	70
All groups	35,755	23,144	12,611	35

*Includes firms in business in 1939 and firms entering business between 1939 and 1960

Bean Automotive

- *Poor location leading to poor sales
- Lack of capital to improve location

Roy Drug

- *Poor location
- Inability to adjust to changing character of customers
- Personality clashes with suppliers

Davis Service Station

- *Unfavorable lease based on production
- Expansion into an area where the operator lacked experience
- Imprudent extension of credit
- Economic conditions--cutthroat competition

White's Grocery

- *Chainstore competition
- Operation of the business as a sideline
- Inattention to credit

Glass Dry Cleaning

- *High-cost operations
- Unsatisfactory used equipment
- Unjustified cash drain in the form of salary

Harris Gasoline

- *Shortage of equity capital
- Fundamental inability of the business to earn a "living" for two owners
- Imprudent extension of credit

Vance (cement block manufacturer)

- *End of a short-run economic advantage
- Operation of the business as a sideline

Cora's Novelties

- *Unsatisfactory lease--poor health of the operator brought on by the condition of the building
- Scale of enterprise--too small to permit even one employee
- Loss of free parking when parking meters were installed

Rise Enterprises

- *Low sales volume
- Insufficient demand

White's Hardware

- *Low sales volume
- Competition with established store
- Imprudent extension of credit

The first of these cases is presented more fully below. All are discussed in detail in the full report.

A CASE OF TOO RAPID EXPANSION

The Doss Manufacturing Company (machine tools) failed after 10 years of operation under Mr. Doss. The owner had a high-school education, about 10 years' experience as a tool and die maker, and several years' experience as supervisor of the business before he bought out the previous owner.

His assistant was a graduate engineer with several years' experience in general contracting work. Most major policy decisions were made by Mr. Doss after consultation with the engineer.

- The Trouble Begins

During the 10 years that Mr. Doss directed the business, sales increased about tenfold and earnings rose rapidly, although they did not keep pace with the increase in sales. The business grew faster than could be supported by earnings. Additional credit, both from suppliers and from local banks, was injected into the business.

At the time of failure, suppliers were deeply involved in the debt structure, and the firm was more than $200,000 in debt to a bank. The company was engaged in filling a large order for a national concern in a neighboring State.

- The Collapse

The immediate cause of failure was the calling of the $200,000 loan by the bank. Mr. Doss could not pay his bills, and the plant closed. His bonding company shifted the project to another company.

Mr. Doss claimed that the action of the bank in calling his loan was in violation of his loan agreement. He further maintained that if the bank had complied with its original agreement with him, the business would not have failed.

He felt certain that his debts, although out of proportion to his net worth, would have been retired in the ordinary course of business. As a matter of fact, the bonding company later sued the bank for unnecessarily causing the surety to perform, and collected a part of its loss.

- An Analysis

Mr. Doss's company was undercapitalized. As in many such cases, the situation had developed gradually as the business expanded. The owner estimated, however, that the net worth of the business immediately before the last contract was negotiated was about half a million dollars.

In view of this, it appears that the action of the bank must be given top billing in this failure.

A contributing factor was the behavior of Mr. Doss in his financial crisis. Some observers believed that if he had applied himself with vigor to the financial problem at the time of the bank's action, complete failure of the business could have been avoided. Whether the firm could have continued to survive with such a degree of undercapitalization is a matter of conjecture. But Mr. Doss was known to have been making plans designed to improve his financial position.

- The Outcome

Mr. Doss lost neither his business reputation nor his entire personal property. The firm was incorporated, but he had signed as an individual on the bond. Still, almost all his substantial personal property was left after the final settlement.

It was generally thought that he could reenter the toolmaking business if he wished, and that he would be able to obtain capital from outside sources. Within a year, he became general superintendent for a large manufacturing firm.

RECOMMENDATIONS

The following recommendations were developed from the findings of the study.

- The public should be aware of the risks as well as the rewards of private enterprise, especially in small business.

- A professional counseling program for both active and prospective small business operators is needed. It was the opinion of the researchers that some of the failures could have been avoided only by not starting the business. Preoperative counseling might have dissuaded most of these failure-bound individuals from entering business.

- The collection of both statistical and descriptive data on small business failure should be encouraged. State and local organizations especially should be urged to gather this information--including statements from businessmen who have failed. A comprehensive study would then be possible.

- Psychological and social research into the impact of business failure on personal and social relations should be encouraged.

ABOUT THE STUDY

One section of the report presents statistical tables, with analysis, concerning various aspects of business instability and failure in Alabama from 1939 to 1960.

A second part of the study was an investigation of individual failures. The principals were interviewed whenever possible. In addition, their suppliers, competitors, bankers, landlords, and friends were asked for comments on the circumstances surrounding the business operation, particularly just before the failure.

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CASES IN POINT

Case Studies for Depth Penetration

Section

THE CASE METHOD OF STUDY

What is the case method? The case method is a teaching device that helps the student learn through exercising the reasoning and decision-making processes. This can be contrasted with other popular teaching techniques which place stress on learning (or memorizing) an accumulation of past knowledge on a given subject. The case method stresses thinking rather than memorizing; it is a dynamic or active method rather than a passive one.

What is a case? A case is a description of an actual or true-to-life business situation. It is a statement of facts, opinions, and judgements -- in short, it is a problem.

The case method is particularly useful in teaching businessmen because it utilizes real, practical problems rather than abstract concepts. Properly used, it provides a realistic environment that causes the participant to become involved and holds his interest. It provides experience in performing essential parts of the administrative tasks without incurring the penalties of a wrong decision on the job. It develops within the individual the process of making decisions, and forces him to think analytically and constructively.

The student also learns the value of group discussion and analysis. Each member of the case discussion group contributes from his unique experience, and each gains from the others. The group knowledge and experience will exceed that of any individual participant -- including the instructor.

The following check-list is suggested as an outline procedure for conducting case study and analysis:

Suggestions for Case Study

1. Read the case carefully for general content.

2. Arrange the facts of the case in order of importance.

3. Recognize and define the major problem(s) that need solution.

4. Analyze the problems and their relative importance.

5. Search for and establish alternative solutions.

6. Select the most desirable of the appropriate solutions.

7. Analyze your probable solutions -- set up the pros and cons of solutions, giving value to each.

8. State your choice, decision, or final conclusion -- be prepared to defend it.

9. Stipulate the plan or plans for implementing the decision.

SPORTY CARPET COMPANY

Background

History

In 1942 Mr. John Liberal purchased a carpet business in a metropolitan city in Oklahoma. Mr. Liberal operated this business as a sole proprietorship until 1946 when it was incorporated as the Sporty Carpet Company, Inc. The primary purpose of the incorporation was to obtain additional funds with which to expand the business. The firm entered the wholesale carpet field, in addition to the retail field, in 1948 with the funds obtained from the incorporation. The organization continued to sell carpet both at wholesale and at retail until its failure.

Location

The business was located on a main street leading to the downtown area, about 25 blocks from central downtown. Numerous furniture, appliance, and carpet stores were located within a few blocks of the business. Most of the houses in the surrounding residential area were in the $8,000 to $15,000 range. The building which housed the business is quite large for a carpet outlet, is constructed of red brick, is in very good repair, and is attractive. The store frontage encompasses almost one-half block, and the store is 50 feet deep. However, only about one-half of the building front contains plate-glass windows.

Another Outlet and Its Failure

A few years after the company was incorporated, Mr. Liberal invested a part of the corporation's money in a retail carpet store in another metropolitan city in Oklahoma. Most of the capital stock, however, was owned by individuals located in the second city. Poor management control by the salaried management reportedly caused the failure of this outlet a few years after it was established. Although the investors lost heavily, they did not go through the bankruptcy court.

[1]This case was taken from Case Studies in Business Success and Failures prepared by Oklahoma State University under the Small Business Administration research grant program. It may be reproduced locally. If material is reprinted, credit to Oklahoma State University and to the Small Business Administration would be appreciated.

In the four years preceding the failure of the Sporty Carpet Company, the business was about evenly divided between wholesale and retail sales. Reportedly, the retail division netted more than twice as much profit as the wholesale division. The incorporators, however, believed that it was wise to continue the wholesale operation because of the contacts made that helped the retail operation and because of a sense of obligation to some of the firms which they supplied. So even though profit-wise the wholesale operation was not as lucrative as the retail operation, it was continued. As a matter of fact, in most years the wholesale division did well just to break even.

Recession and Failure

Industry-wide, 1951 and 1952 were poor years. Retail stores throughout the nation were reportedly overstocked with inventory. During these years people did not seem to be interested in carpeting. The result was lower sales, high inventories, and slow turnover. Prior to this time Sporty Carpet Company's financial position, although not strong, was such that it continued to operate profitably. This industry-wide recession put the business in an embarrassing financial position from which it never fully recovered.

The failure of the other business, the recession, and the withdrawal by Mr. Liberal of a large amount of money from the firm in 1954 put such a strain on the business that it succumbed in mid-1955. The firm's three principal unsecured merchandise creditors filed a petition for involuntary bankruptcy. Amounts owed to these three firms was about one-half-of the outstanding liabilities of the Sporty Carpet Company. At the time of bankruptcy the firm's balance sheet showed assets of $130,000 and liabilities of $200,000. Liabilities of $147,000 were unsecured. At the same time, Liberal took personal bankruptcy with assets of $10,500, of which the sum of $8,500 was claimed as exempt, and liabilities of $225,000, of which the sum of $190,000 was unsecured.

Organization

General Structure

The business was organized as a corporation and operated as a combination wholesale-retail carpet firm during most of its existence. Four individuals invested money in the corporation. They were the officers; namely, Mr. Liberal, the president; Mr. R. L. Joker, the vice-president; Mr. L. G. Conservative, the secretary-treasurer; and Mr. J. D. Robin, the director.

Key Personnel

John Liberal was born in Oklahoma in 1905. He completed high school and worked for a time in Oklahoma. At the age of 23 he moved to Kansas City, where he was employed by a furniture manufacturing concern for 15 years. A benefactor then sold him a retail furniture store at a token price. Liberal operated the business as a proprietorship for four years. This period of time was spent primarily in learning the carpet business. Liberal took advantage of every opportunity to learn about carpets from manufacturers and distributors. He was able to make enough profit to live conservatively and to keep the business on its feet.

During the time Liberal was sole owner, he was very conservative. With the incorporation of the business, however, he began gradually to improve his standard of living. He became a great sports enthusiast and actively supported the local university's sports program. As a member of the Quarterback Club, he helped to support some of the football players by hiring them to work in the business. An avid golfer, he spent many hours a week on the local golf course playing with bankers, professional men, and other successful men of the city. He developed a large circle of friends. Liberal frequently left the business for extended periods of time to attend various golf tournaments throughout the country as a spectator.

Liberal is an easy-going type of individual from outward appearance, but he is very aggressive. He became friendly with many of the executives of local oil companies and succeeded in getting several large contracts for carpet installation from them. The consensus of opinion of those interviewed is that Liberal probably knows more about carpets and their installation than any other individual in the city. He is thought to be an extremely honest and straight-forward individual.

L. G. Conservative, the secretary-treasurer of the corporation, had a background in retail furniture and carpet sales. Conservative began working for Liberal shortly after he opened the retail store. He worked as a salesman until the time of incorporation when he borrowed money to invest in the stock of the business. He had just succeeded in paying off this loan a few months prior to the failure of the business. According to knowledgeable individuals interviewed, Conservative was more attentive to the business than Liberal. Conservative said he was secretary-treasurer of the organization in name only, and his primary responsibility was for sales. He said he did not know the firm was near bankruptcy until a petition was filed by the major creditors.

Operation

Financial Difficulties

The following figures were derived from an analysis of the 1951 and 1952 financial statements of the Sporty Carpet Company. Where available the average ratios for businesses of this type are shown. These averages are based on the Retail Merchant's Association publications for 1951.

	RMA 12-31-51	SPORTY 12-31-51	SPORTY 12-31-52
Current Ratio	1.74-1.00	1.29-1.00	1.34-1.00
Inventory to Working Capital		224%	187%
Stock Turnover		4.4	2.7
Net Sales to Inventory	8.9-1.0	5.8-1.0	3.7-1.0
Average Collection Period		54 days	92 days
Total Liabilities to Net Worth		169%	172%
Net Profits to Net Sales (after taxes)	1.6%	.6%	1.2%
Net Profit to Net Worth	11%	3%	5%
Working Capital		$80,700	$101,600

The inventory-to-working-capital percentage is especially important. Conservative bankers are reluctant to loan money to this type of business when inventory exceeds working capital by more than 75 percent. Also, the excess of total liabilities over net worth is an indication of under-capitalization. When these facts were made known to the bank management which was loaning money to the Sporty Carpet Company, it immediately decided to grant the business only secured loans thereafter. Accounts receivable were pledged to the bank as part security. Sales contracts represented the other portion of the security. In 1955 the bank, which was the major source of financing for the company, sent a man out to audit the Sporty Carpet Company books. This decision was somewhat unusual in that this was the first audit made, even though the bank had been doing business with the Sporty Carpet Company for a number of years. The audit showed fewer accounts receivables on the books than had been pledged to the bank. Immediately the bank demanded additional collateral for their loans. When this information became known to the principal merchandise creditors, they almost immediately filed a petition for involuntary bankruptcy. The monthly balance of loans outstanding to the bank frequently exceeded $100,000.

Most of the merchandise obtained by the company was purchased on open account. At the time of bankruptcy, the unsecured credit of the firm was three times as large as the secured credit. The reliance upon short-term loans caused some difficulty to the firm in meeting its obligations promptly. Much of the money was tied up in inventory in order to perform the wholesaling function. The large inventory in put a strain on the working capital, causing the business to be constantly short of operating funds.

Advertising

Newspaper advertising by the firm represented less than one third of the total advertising expenditure. The major expense was for TV advertising. Liberal had a golfing buddy who was a sportscaster for a local television station. Despite protests from the TV station personnel, Liberal decided to sponsor a five-minute evening program of sports news. Television representatives told Liberal this would not be effective advertising, and a period of time proved that it resulted in few additional sales. According to studies, women are more likely to initiate action that results in carpet sales than men. Few women watch sports news programs so that the appeal was directed to the wrong audience. Liberal was never convinced of the misdirection of the advertising appeal and continued to spend money almost uselessly sponsoring this program.

Misuse of Working Capital

During the year prior to the bankruptcy, Liberal withdrew about $26,000 from the business other than his regular drawing account. Marital difficulty, which ended in a divorce, brought about the withdrawal. This money was paid as a part settlement brought about by divorce proceedings. Shortly after his divorce, Liberal remarried. The withdrawal of $26,000 from the firm, which was already short of working capital, was disastrous.

The firm had to support four families; namely, those of the officers of the corporation. In addition, all salesmen were paid on a straight salary. The business maintained its own carpet workroom, and this operation proved to be much more expensive than it should have been. Altering of carpet pieces consumed too much time and often had to be redone because of faulty workmanship. The supervisor of the workroom was incapable and hired workmen who were highly overpaid in terms of their proficiency. The loss incurred on workroom operations cut heavily into profits.

Causes of Failure

Undoubtedly one of the first mistakes made by the firm was its entry into the wholesale field. None of the officers had any experience in this area. Competition is often particularly severe because many carpet manufacturers circumvent and sell directly to retailers. Because of this practice the margin of profit available to wholesalers is frequently extremely small. As a result, many carpet wholesalers are forced to rely on large volume in order to make operations profitable. Lack of wholesaling experience brought about the maintenance of an excessive inventory that tied up funds badly needed for working capital. To obtain funds for continued operations, the firm was forced to borrow against the inventory. The interest paid on such borrowed funds naturally decreased profits.

Liberal's insistence upon sponsoring the local sports news TV program proved to be sheer foolishness. Had he viewed this problem logically, he would have undoubtedly realized the futility of such advertising effort. Though sponsorship of the program was evidence of Liberal's belief that friends should aid one another, it was an extremely expensive undertaking; and the benefits to the firm were few.

The idea of paying salesmen on a straight salary basis is not well accepted by progressive firms. To insure adequate production by salesmen, it is generally agreed that some form of commission payment is desirable. Conservative was emphatic in stating that several of the employees of the business were highly overpaid. One or two salesmen accounted for most of the sales. Others received the same salary whether or not they sold anything.

If Liberal had continued to operate the corporation in much the same manner as he had operated the proprietorship, the firm would probably be in operation today. Liberal left too many major decisions to other officers and employees. He spent entirely too much time and money attending various sports events. Thus, lack of attention to the business and the withdrawal of funds from the business were the major stumbling blocks to success.

SUGGESTED INCUBATION ASSIGNMENT

I. Visit your local library or branch or regional SBA office and familiarize yourself with its publications on management, marketing, and retailing and service trades. Check those having a specific application to small business.

Secure and study the following SBA publications:

> Problems of Small Retailers, SBA-MRS No. 9
> Small Business Success and Failure Cases, SBA-MRS No. 58
> Essential Personal Qualities for Small Store Managers, SBA-Small Marketers Aid No. 46

II. List several advantages (business or personal) which you believe you enjoy as a small independent, but which you might not have as a manager of a syndicate or chain outlet.

List several disadvantages (business or personal) which you face in meeting competition from larger organizations.

Can any of these limitations be overcome by cooperative effort or other kinds of action?

Draw up a list for your own edification containing the following items:

A. The hours you spend per week in your business.
B. The factors, both personal and impersonal, which you feel are necessary for success in your business line.
C. A rough indication of the time which you spend in a week on business functions -- Example: 15% selling to customers; 25% supervising staff; 10% planning advertising; and so forth.

   Check those elements in (C) that you would classify as:

   1. Doing the job
   2. Managing the job

D. Which of these two elements claims the greatest portion of your time and attention?
E. What should you do and/or can you do about it?

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SMALL BUSINESS ADMINISTRATION
LISTING OF FIELD OFFICE ADDRESSES

*Boston, Massachusetts 02210
Sheraton Building
470 Atlantic Avenue

● Augusta, Maine 04330
114 Western Ave.

● Concord, New Hampshire 03301
18 School Street

● Montpelier, Vermont, 05601
79 Main Street

● Providence, Rhode Island 02903
611 Smith Building
57 Eddy Street

*New York, New York 10004
42 Broadway

▲ Buffalo, New York 14203
448 Ellicott Sq. Bldg.
295 Main St.

● Hartford, Connecticut 06103
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450 Main St.

● Santurce, Puerto Rico 00908
San Alberto Condominio Bldg.
1200 Ponce de Leon Avenue

● Syracuse, New York 13202
Chimes Building
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▲ St. Thomas, U. S. Virgin Islands 00802
P. O. Box 806

*Philadelphia, Pennsylvania 19107
Jefferson Building
1015 Chestnut Street

● Newark, New Jersey 07102
10 Commerce Court

● Pittsburgh, Pennsylvania 15222
Fulton Building
107 6th Street

* Richmond, Virginia 23226
P. O. Box 8565
1904 Byrd Ave.

● Baltimore, Maryland 21202
521 Calvert Building
Fayette & St. Paul Streets

● Charleston, West Virginia 25301
3000 U. S. Court House & Fed..Bldg.
500 Quarrier Street

● Charlotte, North Carolina 28202
Cutter Building
201 S. Tryon Street

● Clarksburg, West Virginia 26301
Old Post Office Building
227 West Pike Street

● Columbia, South Carolina 29201
1801 Assembly Street

● Washington, D.C. 20417
1325 K Street, N. W.

*Atlanta, Georgia 30303
90 Fairlie St, N. W.

● Birmingham, Alabama 35203
New 1st Fed. Savings & Loan Bldg.
2030 1st Avenue North

● Jackson, Mississippi 39201
322 U. S. Post Office & Courthouse Bldg.
Capital & West Sts.

● Jacksonville, Florida 32202
47 West Forsyth

● Knoxville, Tennessee 37902
233 West Cumberland Bldg.
301 West Cumberland Ave.

● Miami, Florida 33130
912 Federal Office Bldg.
51 S. W. 1st. Ave.

● Nashville, Tennessee 37219
Security Federal Savings & Loan Bldg.
500 Union Street

*Cleveland, Ohio 44113
Standard Building
1370 Ontario Street

● Columbus, Ohio 43215
Beacon Building
50 West Gay Street

● Louisville, Kentucky 40202
1900 Commonwealth Building
Fourth and Broadway

*Chicago, Illinois 60603
430 Bankers Building
105 West Adams Street

● Des Moines, Iowa 50309
850 Insurance Exchange Bldg.
Fifth and Grand Avenue

● Indianapolis, Indiana 46204
721 Farm Bureau Insurance Building
130 East Washington Street

● Madison, Wisconsin 53703
Commercial State Bank Building
114 North Carroll Street

*Minneapolis, Minnesota 55402
Lewis Building
603 Second Ave. South

● Fargo, North Dakota 58102
300 American Life Bldg.
207 North Fifth Street

● Sioux Falls, South Dakota 57102
Leaders Building
109½ North Main Avenue

*Kansas City, Missouri 64106
911 Walnut Street

● Omaha, Nebraska 68102
7425 Federal Building
215 North 17th Street

● St. Louis, Missouri 63103
2469 Federal Building
1520 Market Street

● Wichita, Kansas 67202
215 Board of Trade Building
120 South Market Street

● *Dallas, Texas 75202
United Fidelity Life Bldg.
1025 Elm Street

● Houston, Texas 77002
802 Federal Office Bldg.
201 Fannin St.

● Little Rock, Arkansas 72201
377 Post Office and Courthouse Bldg.
600 W. Capital Avenue

● Lubbock, Texas 79401
204 Federal Office Building
1616 19th Street

● Marshall, Texas 75670
Marshall National Bank
101 East Austin Street

● New Orleans, Louisana 70130
729 Federal Office Bldg. (South)
610 South Street

● Oklahoma City, Oklahoma 73102
807 U. S. Post Office Bldg.
3rd and Robinson

● San Antonio, Texas 78204
412 Kallison Building
434 So. Main Avenue

*Denver, Colorado 80202
Railway Exchange Building
909 17th Street

● Albuquerque, New Mexico 87101
102 U. S. Courthouse
Fifth and Gold Streets, S. W.

▲ Casper, Wyoming 82601
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● Salt Lake City, Utah 84101
520 Kearns Building
136 South Main Street

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● Portland, Oregon 97205
330 Pittock Block
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▲ San Diego, California 92104
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*Detroit, Michigan 48226
232 West Grand River Avenue

▲ Marquette, Michigan 49855
Northern Michigan College
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Public Service Center Bldg.

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- GREY — The Lesson Plan

- RUST — The Presentation

- BUFF — The Visual Aids

- GREEN — The Supply Department

- YELLOW — Cases in Point

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