



*Tired Of Working So Hard For So Little?
Why You Are Not Making Money On New Bike Sales!*
Tele-Seminar May 18, 2006
7:00 PM CDT

Are you wondering why you aren't making the money you should be? Did you know the "typical" bike shop doesn't make money on the sale of new bicycles?

Supporting Article: *NBDA Cost of Doing Business Trending Analysis 1993 – 2005* will be sent to all participants, and will be available in the Bike Profits Members Area as a PDF file.

NBDA Cost of Doing Business Survey

The National Bicycle Dealers Association (NBDA) has been conducting Cost of Doing Business surveys for the better part of two decades.

- This unique research program for U.S. bicycle shops represents the most-up-to-date comparative financial performance information available anywhere.
- The Cost of Doing Business studies are an invaluable resource designed as an easy-to-understand tool for bicycle shop owners and managers to evaluate their own business operating results so that they can identify strengths and weaknesses and more importantly take advantage of opportunities and improve profitability.
- To order your copy visit www.nbda.com

The Numbers: The Cost of Doing Business (CODB) survey reports cover key performance measures in three areas: profitability, productivity and financial management.

- Most of the financial performance indicators included in the CODB reports are on the basis of medians rather than averages or means.
- Unlike the mean, the median is not distorted by a small number of unusually high or low values that are reported by the panel of retailers and included in the sample.
- The median represents the mid-point of the figures for a particular measure, with one-half of the responding bicycle shop firms reporting figures above, and one-half below.
- Most of the financial performance indicators are expressed as percentages of total revenue.



Bicycle Shop Reporting Segments

The CODB survey is organized into 14 reporting segments, as follows:

- All Respondents
- High Profit Firms
- Total Company Revenue:
 - Under \$300,000
 - \$300,000 to \$499,999
 - \$500,000 to \$1 million
 - Over \$1 million
- Number of Stores:
 - Multiple Store Firms
 - Single store Firms
 - Single Store Firms With Under 2,500 Square Feet Selling Space
 - Single Store Firms With 2,500 Square Feet Selling Space and Over
- Region:
 - Northeast
 - North Central
 - South
 - West

This CODB Analysis

We have focused this CODB analysis on the following 6 out of the total of 14 reporting segments:

- All Respondents
- High Profit Firms
- Total Company Revenue:
 - Under \$300,000
 - \$300,000 to \$499,999
 - \$500,000 to \$1 million
 - Over \$1 million

For **All Respondents** and **High Profit Firms** we developed a trending report that includes the following four financial categories for comparison of CODB data from seven studies, 1993, 1995, 1997, 1999, 2001, 2003 and 2005 as conducted over the last 12-years:



- Sales Data
 - Total Revenues Per Store

- Margins And Turnover
 - Bicycles
 - Initial Markup at Retail
 - Gross Margin
 - Inventory Turnover
 - Gross Margin Return on Inventory (GMROI)

- Total Operating Expenses
 - Gross Margin to Total Operating Expenses

- Net Operating Profit (or Loss)

What We Learned:

U.S. Specialty Bicycle Retail Typical Gross Margin On Bicycle Sales;
 Typical Operating Expenses; Typical Operating Profit
 National and High Profit Stores

	1999		2001		2003		2005	
	National	High Profit	National	High Profit	National	High Profit	National	High Profit
1. Bicycles*								
a. Initial Markup	40.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0
b. Realized gross margin	36.0	36.1	36.0	36.2	37.0	36.1	38.0	37.4
2. Total Operating Expenses**	37.7	34.7	39.9	33.9	42.5	35.6	43.3	37.5
3. Bicycle Gross Margin to Operating Expense	-1.7	1.4	-3.9	2.3	-5.5	0.5	-5.3	-0.1
4. Net Operating Profit**	4.8	9.6	3.7	9.9	1.8	7.0	2.1	8.3

*Bicycles percent of retail selling price.

**Total Operating Expenses and Net Operating Profit percent of total annual revenue.

Source: National Bicycle Dealers Association (NBDA) Cost of Doing Business Study reports.

Sales Data

Table 1 shows the growth in revenue per store for All Bike Shops from a median of \$327,154 in 1993 to a median of \$549,000 in 2005.



Table 1.
All Responding Bike Shops: Median or Typical Total Revenue

	1993	1995	1997	1999	2001	2003	2005
Total Revenue per Store	\$327,154	\$402,500	\$458,122	\$411,688	\$500,000	\$450,000	\$549,000
Variance year to year		\$75,346	\$55,622	(\$46,434)	\$88,312	(\$50,000)	\$99,000
Variance Year to year		23.0%	13.8%	-10.1%	21.5%	-10.0%	22.0%

Source: NBDA Cost of Doing Business Reports

This revenue growth over 12-years for All Bike Shops totals \$221,846, which is about double the rate of inflation in the U.S. over the same time frame.

Margins: Bicycles

We have focused specifically on new bicycle sales because this represents the biggest single merchandise category for bicycle shops, with 47% to 49% of total annual revenue.

- The single biggest challenge
- The single biggest opportunity

Table 2 shows the initial markup (or mark-on), the realized gross margin and the gap between what gross margin bicycle shops wanted to achieve, and what they actually realized on the sale of new bicycles over the last 12 years.

Table 2
All Responding Bike Shops: Median or Typical Initial Markup to Gross Margin: Bicycles

	1993	1995	1997	1999	2001	2003	2005
Initial Markup	36.0%	37.0%	38.0%	40.0%	40.0%	40.0%	40.0%
Realized Gross Margin	33.0%	34.0%	34.4%	36.0%	36.0%	37.0%	38.0%
Variance	-3.0%	-3.0%	-3.6%	-4.0%	-4.0%	-3.0%	-2.0%

Source: NBDA Cost of Doing Business Reports

- The gap between initial markup and realized gross margin has remained between -3% and -4%
- 2005 the gap improved by 1% to -2%, trending in the right direction
- 2005 the median realized gross margin of 38% - the highest it has been over the last 12 years
- The initial markup of 40% is by itself problematical because for too many bike shops it falls below the cost of doing business, or total operating expenses.



Turnover: Bicycles

Table 3 shows the typical turnover for bicycle inventory.

Table 3
All Responding Bike Shops Median or Typical: Bicycle Inventory Turnover

	1993	1995	1997	1999	2001	2003	2005
Bicycle Inventory Turnover	2.8X	2.6X	2.5X	2.6X	2.5X	2.5X	2.5X

Source: NBDA Cost of Doing Business Reports

- Bicycle inventory turnover has been stuck at 2.5 turns per year since the beginning of this decade
- Turnover of 3.0 contributes to actually making a profit on the sale of new bicycles

Realized Gross Margin Bicycles vs Total Operating Expenses

Table 4 shows realized gross margin on the typical sale of new bicycles against the typical total operating expenses

- The shortfall, which equates to the typical loss on the sale of new bicycles.

Table 4.
All Responding Bike Shops Median or Typical:
Bicycle Gross Margin; Total Operating Expense; Profit or Loss

	1993	1995	1997	1999	2001	2003	2005
Gross Margin: Bicycles	33.0%	34.0%	34.4%	36.0%	36.0%	37.0%	38.0%
Total Operating Expenses	36.7%	35.4%	36.6%	37.7%	39.9%	42.5%	43.3%
Profit or Loss	-3.7%	-1.4%	-2.2%	-1.7%	-3.9%	-5.5%	-5.3%

Source: NBDA Cost of Doing Business Reports.

The Phillips Rule. Harley Phillips, former President of the NBDA and retired bicycle storeowner spent the better part of 25-years educating bike shop owners and managers about the simple rule that "...you never sell anything at retail below your cost of doing business!"



Net Operating Profit (or Loss)

Table 5 shows the typical store operating margin, total operating expenses and net operating profit for all reporting bike shops.

Table 5.
All Responding Bike Shops Median or Typical:
Store Operating Margin; Operating Expenses; Net Operating Profit

	1993	1995	1997	1999	2001	2003	2005
Operating Margin	41.4%	40.3%	42.3%	42.5%	43.5%	44.4%	45.3%
Operating Expenses	36.7%	35.4%	36.6%	37.7%	39.9%	42.5%	43.3%
Net Operating Profit	4.7%	5.0%	5.8%	4.8%	3.7%	1.8%	2.1%

Source: NBDA Cost of Doing Business Reports.

The typical bike shop generated a relatively modest 4.7 to 5.8% operating margin in the 1990’s, but starting with 2001 net operating profit trended downward to the current 2% level. By comparison high profit stores generate three to four times this level of net operating profit.

High Profit Bicycle Shops

- According to the NBDA CODB High profit bicycle shop firms are those in the upper 20% to 25% based on before tax return on assets.¹
- The National Sporting Goods Association (NSGA) defines high profit firms as those in the upper 25% based on net profit before tax to total revenues.²
- In either case the high profit bike shops in the U.S. are the best retail performers in the channel. They stand out because of their profitability and productivity.
- In the 2005 CODB 19% of the responding firms were identified as being high profit bicycle shops.

Sales Data

Table 6 shows the revenue growth of high profit bike shops over the last 12-years, from \$392,594 in 1993 to \$799,000 in 2005.

¹ 2006-2007-NBDA Financial Survey: Cost of Doing Business Survey for Specialty Bicycle Retailers, page 2.

² 2004-2005 NSGA Cost of Doing Business Survey, page 4.



Table 6.
High Profit Bike Shops: Median or Typical Total Revenue

	1993	1995	1997	1999	2001	2003	2005
Total Revenue per Store	\$392,594	\$416,427	\$447,083	\$489,818	\$558,403	\$662,066	\$799,000
Variance year to year		\$23,833	\$30,656	\$42,735	\$68,585	\$103,663	\$136,934
Variance Year to year		6.1%	7.4%	9.6%	14.0%	18.6%	20.7%

Source: NBDA Cost of Doing Business Reports

Margins: Bicycles

- High profit bike shops show the same initial markup to realized gross margin trend as all-responding bike shops as shown in Table 7.
- The whole of the channel has been stuck at a median, or typical initial markup of 40% on new bicycles for the last 6-years
- Typical realized gross margins have been consistently between 36% and 38% over the same 6-years (from 1999 to 2005).
- We believe increasing initial markup and realized gross margin on sales of new bicycles represents an opportunity for growing retailer revenue and profitability going forward.

Table 7.
High Profit Bike Shops: Median or Typical Initial Markup to Gross Margin: Bicycles

	1993	1995	1997	1999	2001	2003	2005
Initial Markup	36.5%	37.0%	38.0%	40.0%	40.0%	40.0%	40.0%
Realized Gross Margin	33.0%	34.4%	35.6%	36.1%	36.2%	36.1%	37.4%
Variance	3.5%	2.6%	2.4%	3.9%	3.8%	3.9%	2.6%

Source: NBDA Cost of Doing Business Reports

- The shortfall or gap between high profit bikes shops typical initial markup and realized gross margin is trending in the right direction
- If the variance reported in 2005 continues to narrow over the second half of this decade.

Turnover: Bicycles

As shown in Table 8, the high profit bicycle retailers came back from a low 2 inventory turns in 1999 to 2.8 in 2001 and 3 turns per year in 2003 and 2005.



This compares to the 2.5 annual inventory turns on bicycles that all responding firms have been stuck at virtually since 1995.

- The additional one-half turn is driving a stronger contribution to an overall stronger net operating profit for the high profit retail stores.

Table 8.
All Responding Bike Shops Median or Typical: Bicycle Inventory Turnover and GMROI

	1993	1995	1997	1999	2001	2003	2005
Bicycle Inventory Turnover	2.4X	2.6X	2.4X	2.0X	2.8X	3.0X	3.0X

Source: NBDA Cost of Doing Business Reports

Realized Gross Margin Bicycles vs Total Operating Expenses

- High profit bike shops have consistently generated profit on the sale of new bicycles for most of the 12-years covered by this analysis, as shown in Table 9.
- The 2005 CODB survey brings with it a concern about high profit bike shops relative to new bicycle profitability.
 - In a year of greatly increased revenue, driven by the sales of more higher priced road 700c bicycles, the typical high profit bicycle retailer reported a slight loss on the sale of new bicycles.
 - This is alarming because it reverses a trend of profitability in the single largest, and some would argue, most important of all the product categories carried by specialty bicycle retailers!

Table 9.
High Profit Bike Shops Median or Typical:
Bicycle Gross Margin; Total Operating Expense; Profit or Loss

	1993	1995	1997	1999	2001	2003	2005
Gross Margin: Bicycles	33.0%	34.4%	35.6%	36.1%	36.2%	36.1%	37.4%
Total Operating Expenses	33.9%	32.7%	34.4%	34.7%	33.9%	35.6%	37.5%
Profit or Loss	-0.9%	1.7%	1.2%	1.4%	2.3%	0.5%	-0.1%

Source: NBDA Cost of Doing Business Reports.

Net Operating Profit (or Loss)

- This is one of the key financial metrics that determines if a bike shop is high profit or not.



- Table 10 shows the 12-year trend in high profit bike shop operating margin, operating expenses and net operating profit.
- All responding bike shops have a typical net operating profit ranging from a high of 5.8% to a low of 1.8% of total revenue
- High profit bike shops have a typical net operating profit ranging from a high of 9.9% to a low of 7.0% over the last 12-years.

Table 10.
High Profit Bike Shops Median or Typical:
Operating Margin; Operating Expenses; Net Operating Profit

	1993	1995	1997	1999	2001	2003	2005
Operating Margin	42.9%	41.9%	44.0%	44.3%	43.8%	42.6%	45.8%
Operating Expenses	33.9%	32.7%	34.4%	34.7%	33.9%	35.6%	37.5%
Net Operating Profit	9.0%	9.2%	9.5%	9.6%	9.9%	7.0%	8.3%

Source: NBDA Cost of Doing Business Reports.

- While the overall net operating profit reported by high profit retailers is impressive, the erosion starting in 2003 with 7.0% and continuing in 2005 with 8.3% is of concern.
- The typical high profit operating margin of 45.8% in 2005 is the highest achieved over the 12-years we have analyzed
- But the operating expense of 37.5% is also the highest over the same time frame.
- There are definitely bicycle retailers in the U.S. that have consistently made a profit on selling new bicycles.
- However, they are probably all in the high profit category which constituted 19% of all bike shops participating in the 2005 survey, leaving approximately 80% of U.S. bike shops generating a consistent loss or at best a breakeven on the sale of new bicycles over the last 7 to 12-years.



In Summary

- The typical bike shop in the U.S. has taken a loss on the sale of new bicycles for over a decade. This is significant for a number of reasons, including the fact that new bicycle sales represent between 47% and 48% of total store revenues.
- Initial markup for new bicycles has remained at a typical 40% for 6-years, from 1999 through 2005. This initial markup appears to be undervaluing most new bicycles, and needs to be reviewed by specialty bicycle retailers to determine what can be done to increase the initial markup and the realized gross margin on new bicycles.
- Some U.S. bicycle shops have made consistent profit on the sale of new bicycles, and are probably classified as high profit bike shops, which constituted 19% of all responding firms to the 2005 Cost of Doing Business survey. This leaves approximately 80% of the typical U.S. bike shops consistently selling new bicycles at a loss, or at best breakeven.
- The typical high profit bike shop has consistently made a profit on the sale of new bicycles. However, in 2005 the typical high profit bike shop reported a slight loss on the sale of new bicycles.
- Retailers need to revisit and adopt *The Phillips Rule* as a part of establishing consistent product pricing policies to increase revenue and gross margins.
- Most bike shops need to focus on increasing inventory turnover on all categories by at least one full turn per year.
- Total operating expenses have increased for the typical U.S. bike shop over the last 12-years, and in particular since the year 2000.
- High profit bike shops have done a better job of controlling total operating expenses, although the last two Cost of Doing Business surveys show a steady increase in expenses.
- The majority of U.S. bike shops, including high profit retailers need to adopt policies, procedures and systems to control and reduce operating expenses.
- The typical high profit bike shop has established the benchmarks that all U.S. bike shops should strive for and set operating objectives from.

Strategic Considerations

Review your pricing policy and determine where you can generate higher margins

Work with and select brands that are not over represented in your market, and are not generally discounted

Make your store the brand

Focus on customers and not products – and on creating individual solutions for clients!