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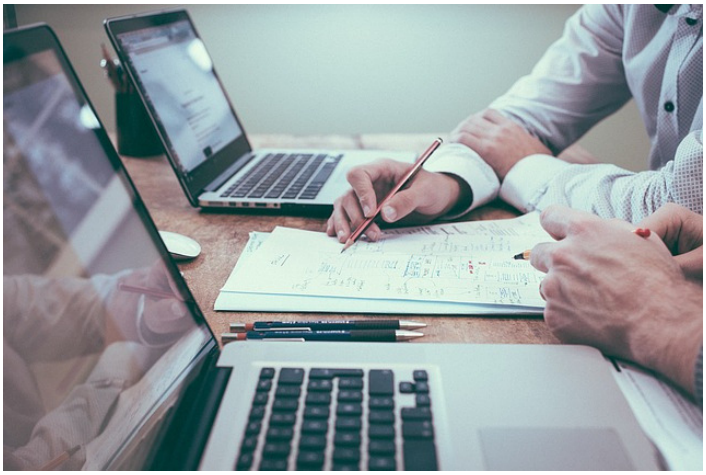
10 METRICS PROVEN TO BOOST DIESEL ENGINE REPAIR SHOP PROFITABILITY

A HIGHWAY & HEAVY PARTS WHITE PAPER

10 METRICS PROVEN TO BOOST DIESEL ENGINE REPAIR SHOP PROFITABILITY



It's always good to make more money, right? But sometimes it's hard to identify strategies for making that goal into reality. This white paper, the RSVP Profit Boosting Boot Camp, aims to help you pinpoint metrics to track that can help your shop really grow. Don't just wish you could increase your profits, learn how to make it happen!

Why Tracking Metrics is Vital to the Success of Your Repair Shop

HHP conducted a nationwide survey and found that the biggest concern amongst shop owners for 2018 is bottom line profitability. Yet with the increase in costs for parts and overhead and the shortage of technicians, many repair shops find themselves not knowing how to give their profits that bump up.

One often overlooked strategy is tracking KPI's (key performance indicators) and other measurables to help determine areas for improvement. In their June issue, Ratchet+Wrench detailed the results of a study they conducted about KPI tracking. A large majority of shop owners who responded claim to routinely track KPI's, and many of them described how these measurements were vital in the overall health of their bottom line. Even more than that, the numbers they published show that shops who tracked and responded to KPI's outperformed those shops that did not.

More than anything, tracking your shop's KPI's and other important metrics will give you a better idea of what your shop is doing right and where money is being lost. It takes the guesswork out of figuring out what is draining your profits. HHP also released a white paper discussing ways to maximize your profits. Visit our previous post to download a copy.

Metrics You Should Be Tracking

Okay, so you want to start tracking your metrics. But what should you look for and how does that help you make decisions about the future of your shop? That's what this series will cover, spending time going into depth about each of the following topics:

Closing Ratio

The closing ratio is the percentage of items from a quote that were actually sold at a given transaction. A higher percentage should indicate higher profits. The danger lies, though, at not questioning why your closing ratio might be high. An estimate that quotes only work the customer requested might have a 100% closing ratio, but the opportunity was lost to sell the client additional work.

Average Order Value

The average order value can be calculated by dividing the total revenue by the number of orders. The resulting figure is how much customers spend on average. This number, too, can be increased by upselling or pointing out additional repairs, but it has its limitations as well.

Overall Gross Profit Margin

Your overall gross profit margin is the revenue minus the cost of goods sold (this does not include operating expenses) all divided by the total revenue. This number helps to measure a shop's success at generating revenue from the cost of parts and labor.

Gross Profit Margin on Parts

This is calculated in a similar way to the overall gross profit margin, but focuses specifically on the revenue generated from parts after the cost has been subtracted. There are some ways to increase this revenue, including increasing markups. This might be the most obvious solution, but it also runs the risk of driving away customers if the prices rise too much. In many cases, another solution might serve your shop better.

Gross Profit Margin on Labor

Again, this is figured similarly to the previous two topics, with the labor cost being subtracted from the labor revenue and then divided by the labor revenue. This number zeroes in on the effect of labor costs to your shop's revenue.

Net Profit Margin

The net profit margin is the revenue minus all costs (goods sold, operating costs, taxes, interest, etc.) divided by the total revenue. Watching trends in net profit can allow a company to better track which practices are working well for them and address those that aren't.

Posted Labor Rate

This number is how much a shop charges for labor. Public perception is that labor rates are too high, but in reality, they are often low, hurting the shop's bottom line.

Effective Labor Rate

This is calculated by dividing the total labor sales by the total labor hours. Raising efficiency is one method to help the effective labor rate, as is re-evaluating the way hours are billed to the customer to ensure accurate estimates.

Productivity

This is best measured by dividing the hours worked by the hours available. This allows you to better evaluate down-time and the amount of work that is actually available for your technicians.

Efficiency

This can be tracked by dividing the hours sold to the customer by the number of hours it actually takes your technician to do the job. A number greater than 1 is ideal, but it's important not to make speed your only goal.

HOW YOUR CLOSING RATIO IMPACTS YOUR SHOP'S PROFITS

How often have you looked at your shop's profits and wished they were higher? As we've mentioned earlier, in 10 Metrics Proven to Boost Diesel Engine Repair Shop Profitability, tracking your key performance indicators (KPI) can help you identify some strategies to actually move your shop towards its future profit goals. Looking at your closing ratio is one such metric that can help.

Closing Ratio Explained

So just what is a closing ratio? Put simply, it is the percentage of items from a quote that were sold at a given transaction. So if you quote a customer 10 different things in a single visit and they purchase 7 of them, the closing ratio would be 70%. So the more items sold in one transaction, the higher the closing ratio will be. It follows then, that with consistently high closing ratios come higher profits.

How to Increase Your Closing Ratio

There are several strategies you can employ to raise your average closing ratio. One of the most important things you can do is focus on how your office staff interacts with customers. This helps you to maximize the value of your resource—your staff. To read more about implementing strategic productivity take a look at our previous blog. In their October 2013 issue, Ratchet+Wrench included an article about how to increase your closing ratio through the way the office staff approach each sale.

As they point out, these staff members are your salespeople, the ones with the ability to sell your services to the customer, and it's important that they go into each customer interaction with that in mind. Rather than just acting as a go-between from the technicians to the customers, have them focus on the customer's needs, to better quote jobs to them. This change in mindset helps close sales.

Another way to increase closing ratios is to close more sales. This might seem obvious, but it takes some strategic planning. It's important to look at which items are selling well and which are struggling. Then try to identify why. Are the salespeople not telling the customers why the jobs are being recommended? Are the additional repairs presented in such a way that makes them seem like you're just trying to get more money out of them? Figuring this out can help you form a plan moving forward.

Upselling, or trying to increase the amount of items a customer purchases, will also help your closing ratio. It can be difficult to convince your customer to add on additional repairs if they come in for something specific. But that's when it's important to have your staff build trust with clients. Let the customer know that the additional repairs quoted are a value to them, whether monetary, safety, or both. Try to avoid making them feel like you're just trying to get more money out of them by selling them unnecessary jobs—show them why those repairs are being quoted to them and why they're actually necessary to the overall health of their engine.

Providing comprehensive estimates to every customer can help with this. Do a thorough inspection and provide them with an estimate that includes the work they came to have done, but also any other repairs you find that are necessary to keep them operating at full potential. Again, don't try and sell them things they don't actually need—this will make them lose trust in your staff and drive them away. Instead, listen to their needs and provide them with an estimate that is in line with their goals. They are more likely to trust the advice and the chances of making the sale increases. This trust will help improve your closing ratios in the present, as well as with repeat customers in the long-term.

Possible Problems with Closing Ratios

While increasing your closing ratios is a good goal, it doesn't mean that it's necessarily increasing your profits. Just because the average closing ratio is high, it doesn't mean that your sales staff is taking advantage of every sales opportunity. It's easy to sell the smaller ticket repairs, especially the ones the customer specifically asked for, but usually the bigger profit comes from bigger repairs. Don't just focus on increasing your closing ratios overall, look at the order types and value to see where you're succeeding and what needs improvement.

So if your closing ratio is lower on the more expensive repairs, you still might have a higher profit margin than closing 100% of the smaller sales. That's why it's important to build trust with your customers. Walk them through why additional repairs are being quoted to them and the value it brings to them in the long run —it might cost them more money now, but it will save them cash in the future. This trust makes it easier to close more of the larger jobs, improving your closing ratio on the sales that can really help your profits.

What Your Closing Ratio Might Indicate About Your Shop

Essentially, it tracks how well your shop is selling itself to potential clients. Monitoring your closing ratio forces you to evaluate not just how well you get clients in the door, but how well you keep them there.

Customers nowadays want to know that the repair work they'll be receiving is quality, and it's your job, or the job of your sales staff, to show them your shop is the one that can provide that. Make sure they get a thorough estimate and explain why you're recommending certain repairs. Customers want to feel in control, so become their trusted advisor. Not only are you more likely to make the sale, but the chance of gaining a repeat customer increases.

WHAT YOUR AVERAGE ORDER VALUE MEANS FOR YOUR SHOP

While it might seem like busywork, tracking your shop's KPI's is actually a vital part of growing your business. As we discussed in How Your Closing Ratio Impacts Your Shop's Performance, we discussed ways to improve your closing ratio and why it's important to monitor. A metric closely related to the closing ratio and just as important to track is the average order value (also called the average repair order).

This number tells you how much on average a customer spends per transaction and can be calculated by dividing total revenue by the number of orders. So, if a shop has a total revenue of $2,000,000 and has 4,000 orders, then the average order value would be $500, meaning that, on average, a customer spent $500 on each transaction made at the shop.

This number can give you insight into how successfully your shop is selling repairs.

How to Improve Your Average Order Value

There are several things to think about when trying to improve your average order value. After interviewing shop owners for their June 2018 issue, Ratchet+Wrench pointed to monitoring closing ratios as a key way to improve the average order value. In this way, it's not just how much each sale is making, but how many sales opportunities the sales staff closes. By tracking both, you get a much clearer picture as to the overall success of the sales team.

They also indicate that having the sales team push to have more billable hours on each order will help push up the average order value.

We'll talk more about labor hours in later on in this white paper.

Some strategies to raise the average order value overlap with those used to improve closing ratios. Building trust with customers plays an equally important role in both the closing ratio and average order value. By fully explaining necessary repairs to customers, and perhaps even showing them the issues on the vehicle directly, if possible, they become more likely to listen to the advice and purchase the recommended repairs. This also aids in building a solid repeat customer base. The more repairs they purchase on any given job, the higher the average order value becomes.

Similarly, presenting the customers with a thorough repair estimate is important to both metrics. By letting a customer know that there are more repairs necessary than what they came in for, you gain the opportunity for them to purchase more services. This, in turn, would help raise your average order value. Again, it's important not to try and sell them things they don't need—customers will often see through this strategy and you run the risk of driving them away. Instead, focus on their needs and the long-term health of their engine. Let them know why the repair has been recommended.

Things to Think About As You Track Your Average Order Value

There are some important things to consider as you begin to track your average order value and what it means for your shop.

The average order value is not an indicator of overall profit, but of how much the customer is spending. Costs are not taken into consideration for this calculation. Evaluating this would emphasize the financial side, which, while important, isn't really what the average order value is meant to do.

Instead, the average order value tracks customer buying trends. You're able to see what customers are historically spending each time they visit your shop and you can use this information as you build a sales plan moving forward. If you're getting a lot of orders, but the average is low, think about ways you could raise that average. On the other hand, if you notice the average order value is high, but there aren't as many orders as you'd like, you might want to evaluate how you can build a repeat customer base or revamp your marketing strategy to bring in new clients. Read our previous post, Creating Powerful Marketing Messages for Your Diesel Repair Shop to learn more about how to effectively market your shop.

Keep in mind that when looking at the average order value, it can be hard to differentiate between a customer who purchases many smaller things as opposed to one large job. It also doesn't take into consideration customers who complete multiple transactions. While this doesn't necessarily directly impact the profit, it could be useful to know when evaluating sales techniques. Gaps like this are why it's important to track multiple metrics. By doing so, you get the entire picture, rather than just guessing at what you think is happening.

GROSS PROFIT MARGIN

A common question business owners want answered is: how do I know if I'm making enough profit to stay open? Earlier, we talked about average order value, which can directly feed into profits, but one metric that can help answer this larger question is your gross profit margin.

Gross Profit Margin Explained

The gross profit margin measures how much money you're making after the costs of goods sold (parts and labor) is subtracted. To calculate: (Revenue – Costs of goods sold) / Revenue. For example, if a shop brings in $1,500,000 of total revenue, but the costs of goods sold is $450,000, then their gross profit margin is 70%.

By monitoring the gross profit margin (usually calculated as a percent) instead of just gross profit, you're better able to track trends in your profits.

Depending on how you want to plan for the future of the shop, the gross profit margin can be broken down by different time frames (week, month, year, etc.) if you're wanting to evaluate the overall profitability, or by job, if you want to see how profitable different types of jobs are. The latter allows you to pinpoint exactly where you might be losing money, while the former focuses more on the big picture.

Why Bother Tracking Your Gross Profit Margin

Like the other KPIs we recommend monitoring, the gross profit margin can tell you several important things. First, it lets you know if you're making enough money in sales to cover your costs. If you're not, it's a good sign that you might need to reevaluate your pricing structure.
It also tells you just how profitable your company is. The higher the gross profit margin, the more profitable a company. Similarly, the gross profit margin allows you to better spot trends in your profitability. You can begin to notice when or where you don't seem to be making as much money and develop a plan to address it.

What Can be Done to Raise the Gross Profit Margin?

There are several different approaches you could try to help raise your gross profit margin, each with its own advantages and disadvantages.

Increase the Price of Parts

This seems like it would be the most obvious solution—increase your parts markup to maximize the amount of money you make on each job. It's true that you don't want to be losing money on parts, so it's important that you're charging the customer at least as much as you paid, if not a little more, to help your own profits.

You should note that there is always a danger in raising your prices. You run the risk of driving away customers if prices rise too much, defeating the purpose of raising them in the first place. Make sure that your prices are still competitive enough to keep customers from taking their business down the street.

Increase Billable Hours

By increasing the numbers of hours sold, you're again increasing the amount of money brought into the shop without incurring any additional costs. It runs a similar risk to raising prices on parts, though. You never want to charge a customer so much that they feel taken advantage of. It won't end up increasing your profits in the long run.

Decrease Costs

By decreasing the costs of goods sold, you're able to raise the gross profit margin while eliminating the risk of alienating the customer. There are several ways you could reduce costs.

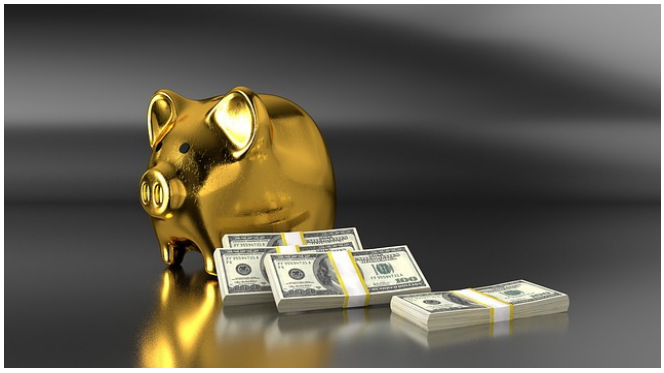
First, you could increase the productivity and efficiency of your technicians. Make sure their time is being used to its maximum potential. Don't lose money due to inefficient systems. We'll discuss how to increase productivity and efficiency in later posts.

You could also try to decrease the amount you spend on parts. Make sure you're getting the best value by shopping around parts suppliers. Ask about discounts for buying in bulk or if they have any sort of preferred pricing (HHP does!). If you purchase only OEM parts, you could look into quality aftermarket options that cost you less but are made to the same standards as OEMs.

Things to Consider

While the gross profit margin does provide a good look at the profitability of you shop, keep in mind that the calculation doesn't include any overhead costs. This means that when looking at the overall profitability, you need to keep these costs in mind—it might seem like you're making a profit based on the gross profit margin, but you also need to make sure you enough money to cover operating costs, non-technician salaries and benefits, taxes, etc.

GROSS PROFIT MARGIN ON PARTS



This time, we're taking a look at you gross profit margin on parts. Very similar to the overall gross profit margin, it's calculated in much the same way, except focusing in on parts: revenue from parts minus cost of parts, then divided by the revenue from parts. This percentage is your gross profit margin on parts. It lets you know how much profit you're making from the sale of parts on the jobs in your shop.

Like the overall gross profit margin, this metric, too, allows you to track trends in profitability. Are they consistent, or are you still losing money on some jobs? Following your gross profit margin on parts lets you identify these places and make plans for future improvements.

Raising Your Gross Profit Margin on Parts

There are quite a few strategies you can employ on your quest to improve your gross profit margin on parts. These include:

Streamline Your Parts Management System

Using an electronic database for your parts management system with a dashboard that allows for real-time updates can help increase the efficiency of your parts department and help you properly price your parts. It also helps you to better understand your various vendors and their pricing systems. Having parts priced accurately is key to improving your gross profit margin on parts.

Understand Profit Numbers by Manufacturer

This will help you make more informed purchase decisions, as you will better know where the best prices are for the various parts you need to stock. It will also help you better decide how many of a given part to order at a time, especially of high performing sales items.

Decide on the Margins You Need for Parts

It's important that you know how much you need to make on each part you sell and price them accordingly. Be systematic about this. Use a parts pricing matrix inserted into your parts management system so that it's accessible when you complete a sale. Making sure each and every part is priced according to the margin you need to make will help increase your overall profits.

Purchase Aftermarket Parts to Increase Margins

Looking into a quality aftermarket supplier, like HHP, can help increase your profits. Aftermarket parts often cost significantly less than their OEM counterparts, allowing for increased savings for you, as well as a higher profit margin. It's good to note as well that aftermarket parts can have just as impressive quality and warranty as those from the OEM.

Work with Vendors

Make sure that you are communicating with your vendors to get any possible discounts. Many have decreased costs for volume purchasing or preferred pricing for repeat customers. Check out our Repair Shop Value Program to learn more about our preferred pricing.

Understand Shipping and Pricing From Vendors

Take a look at the shipping procedures and availability from your vendors. Sometimes one may have a lower price, but that small savings won't save you money in the long run if you're losing money due to repair delays. Be sure that you're getting the best price and the shipping time you need to ensure the repair work gets done in a timely manner. This will keep your customer satisfied and coming back, securing future profits.

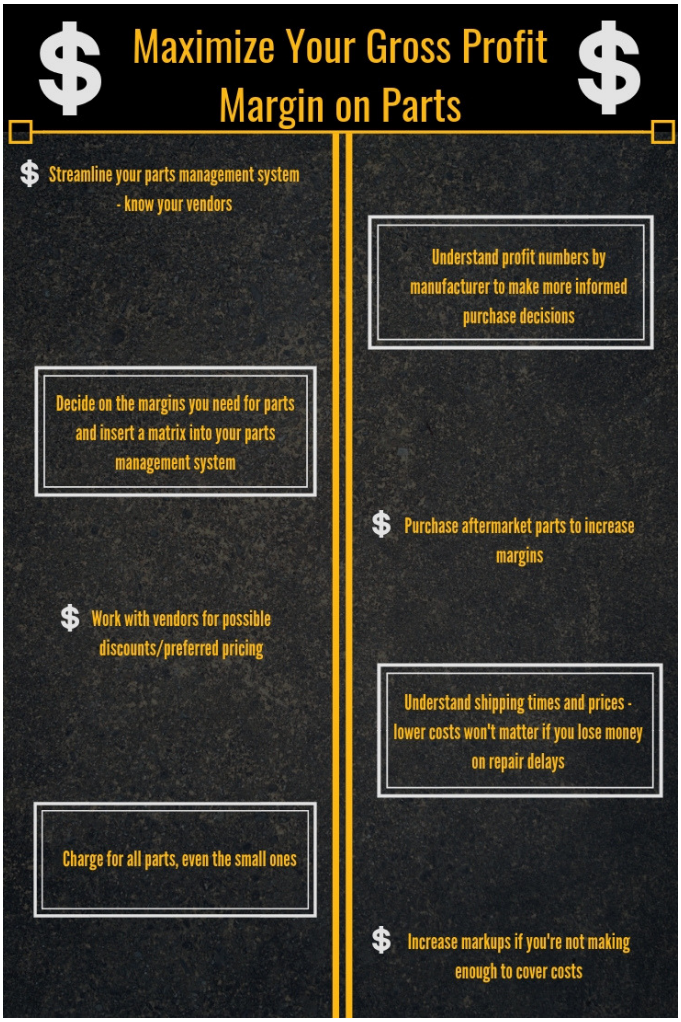
Charge for All Parts

It might seem like a no-brainer. Who doesn't charge for parts? But it's important to make sure that even the small parts are being billed, including bolts and other seemingly unimportant parts that sometimes get thrown in for free. These small costs can add up, and by making sure you charge for them, you'll be surprised to see your profits grow.

Make Sure Your Markups Cover the Costs

This again might seem simple, but make sure the price you're charging the customer is actually indicative of how much it costs you to get the part to them and on their engine. This can prevent you from taking too much of a profit loss.

The infographic below summarizes these ideas:



Some Things to Consider

As we mentioned in the previous post, be careful not to increase your markups too high. Yes, it's important to make money, but you also have to keep the customer in mind. Is your pricing still consistent with industry standards? You don't want to unintentionally drive your customers into the arms of another repair shop.

In March of 2014, **Ratchet+Wrench** published an article in which they spoke with a couple of repair shops on how they track their KPIs. One shop noted that markups might not be the same across the board. Doing this could actually cost you money in the long run. Instead, know what percent profit you need to make on each part and figure your markup accordingly. It's important to be familiar with the price structures of your vendors to help you decide on the proper markups.

While it might seem redundant to track both your overall gross profit margin and your gross profit margin on parts, focusing in on the specifics can give you a clearer picture of what's happening in your shop. This allows you to really note any problem areas, as well as things that have been working well, to better guide your shop to increased profitability.

GROSS PROFIT MARGIN ON LABOR

In the last few sections, we have focused on discussing what you should know in regards to your gross profit margin and your gross profit margin on parts. This post will focus on your gross profit margin on labor.

Combined with your gross profit margin on parts, this is the second part that makes up your overall gross profit margin. Similar to the gross profit margin on parts, this more focused metric allows you to pinpoint what specifically is helping your shop's profitability or what could still be improved.

To help better understand how your labor prices are affecting your profits, calculate your labor profit margin by subtracting the labor costs from the revenue from labor, and then dividing by the revenue from labor.

$$\text{Gross Profit Margin on Labor} = \frac{\text{Revenue from labor - cost of labor}}{\text{Revenue from labor}}$$

It's important to note that your services—labor and expertise—is a big part of what you offer to your customers, and should be priced accordingly.

Improving Your Gross Profit Margin on Labor

Like any KPI, tracking is one thing, but what you really want to know is how to meet your goal or improve current processes. Here are some things that can help you increase your gross profit margin on labor:

Provide Accurate Estimates

In a March of 2014 interview with shop owners who track KPIs, Ratchet+Wrench noted that providing accurate estimates is key to reach gross profit margin goals, including gross profit margin on labor. Customers pay based on estimates, so if you're not quoting the correct number of hours, you're not making as much per job as you should. Work to ensure every estimate is as accurate as possible.

Charge for Every Hour

The Ratchet+Wrench article goes on to point out that you need to be charging for every hour it will take to complete the job. If there are special circumstances that you know will cause the tech to take longer than normal to complete a particular job, charge for it. Every hour your techs are working on an engine that a customer isn't paying for, you're losing money.

Increase Billable Hours

This goes hand-in-hand with providing a proper estimate. The more time your technicians are working on an engine, the more money your shop is making. Charge for diagnostics, streamline efficiency protocols to allow for more billable time, and work on bringing more customers in to help raise the overall number of billable hours you can sell.

Decrease Non-billable Hours

Inversely, you can focus on decreasing the number of hours your technicians spend not working on a job. Evaluate your shop's processes, or create standard processes to help identify and eliminate things that are costing your technicians time and you money.

Make Sure Your Labor Rate is Competitive

As we previously mentioned, the skill and expertise of your staff is a large part of what your customers are paying for, so it's imperative that you're charging an appropriate rate for their time. You want to make sure it's within industry standards, but it's a good opportunity for you to increase profits, as it's not as easy for a customer to look up the cost of shop labor hours as it is for them to find the price of various parts online. Obviously, overcharging can drive customers away, but don't be afraid to charge what your technicians' time is actually worth.

Set a Different Gross Profit Margin Goal on Parts and Labor

Bob Cooper, writing for Elite in July of 2015, urges shop owners to evaluate their gross profit margin goals. He notes that many shop owners follow the margins set by their mentors, but in an age where customers are able to cost compare part prices online easily, that may not be the most profitable thing for your shop. He poses the question: would you rather defend your higher price markups or the cost of your skilled workers? Oftentimes, it's easier to convince a customer of labor costs, and even make them glad to pay them, if they feel that your workers are the best around. Lowering your parts profit margin goals and raising your labor goal to make up the difference can help you to increase sales.

Increase Efficiency

We'll talk more about efficiency in an upcoming post, but as general concept there are some strategies you can employ to help raise your gross profit on labor. Again, evaluate your current shop processes. Are there redundant steps? Places where your workers are losing a lot of time? Think about how each process might be optimized. Can someone else be assigned the task? Is there helpful technology that would cut down on time? Can steps be removed without hurting the overall effectiveness of the process? Thinking about these things can help keep your technicians working smoothly and effectively, allowing the opportunity for more profit on labor.

The following infographic brings these ideas together:

What to Think About When Making Changes to Improve Your Gross Profit Margin on Labor

Often, decreasing non-billable hours is not an employee or technician issue, but a procedural problem. Yes, you'll have the occasional personnel issue, but if it's a consistent problem throughout the shop, take a look at the operating procedure before thinking it's your employees wasting time. You might be surprised to notice inefficient processes or ones that haven't been changed as your shop has. Evaluating and editing these procedures may be the key to fixing time management issues.

Make sure that you're not pushing efficiency so far that you're sacrificing quality. It's true that you want to get things done quickly, but quality is also the key. You'll lose even more time and money if a customer has to come back with a problem on the repair that was rushed than by taking the proper amount of time in the first place. It's all about balance.

Tracking all three of these metrics really paints a clear picture of how and where your shop is making its money and affords you better control of the situation. Once you understand what's really happening, you can make moves to shift areas that need improvement to higher profitability and really evaluate which strategies have helped you reach the numbers you want to see.

INVESTIGATING YOUR NET PROFIT MARGIN

Understanding your net profit margin can be key to understanding your shop's profitability and what you can do to improve it. We've spent some time going through your gross profit margin in our

previous post, and your net profit margin is closely related. This metric is vital to future planning for your shop's profitability.

Net Profit Margin Explained

Your shop's net profit margin tells you exactly how profitable you are after all expenses of operating your business are subtracted. By tracking your net profit margin, not only can you ensure that you're not operating on a loss, but you can better project how your future profits might lay out. You can track trends from month to month, and even year to year to get a clearer idea of exactly what is happening to your money, and if you know that, you can make changes accordingly. All in all, knowledge is the key to boosting your shop's profitability.
To calculate, subtract the total costs (goods sold, operating costs, taxes, interest, etc.) from the total revenue and then divide by the total revenue:

You might have noticed that the last few posts all have similar themes—your profit margins. So why do you need to track another one?

It's true that each of the profit margins have similarities, but each of them is a piece of the larger whole that is your shop's finances. The net profit margin helps capture this whole. Unlike the gross profit margin, the net profit margin does include overhead costs, which can sometimes be forgotten when figuring pricing.

Tracking your net profit margin forces you to evaluate how your overhead costs are impacting your bottom line, rather than allowing a great gross profit margin lead you to falsely believe that your shop is in the green.

Improving Your Net Profit Margin

Like with the gross profit margins we discussed in previous posts, working to improve your net profit margin will directly impact your bottom line. Here are some things to think through as you decide on a course to improve yours.

The Actual Cost of Running a Business

In 2014, Ratchet+Wrench published an interview with a shop owner whose repair shop has been profitable all 33 years it's been open. In this interview, he stated that the most important thing to know about your business is how much it actually costs to stay open and operating every day. Every other number depends on that. According to the article, there is no other way to run a profitable shop without knowing that number.

Once you know your costs, you can easily tell if you're actually making enough money to keep your doors open—and make plans to fix it if you're not. From this base, you can evaluate which areas are costing you the most and take steps to decrease those numbers. This is helpful even if you are profitable. Who doesn't want to cut costs and make more money?

Building Strong Customer Loyalty

That same article also emphasizes the importance of customer relationships. Treating your customers like the valued asset they are is what helps keep them coming back to your shop—and often word-of-mouth is the best marketing your shop can do. And it doesn't cost you anything.

Think about your customer retention rates. If they're lower than you would like them, think about why that might be. Would more thorough estimates help? A more inviting waiting area? Work on building those solid, trusting relationships, and the customers will keep coming back, helping your net profit when they do.

Evaluate Your Marketing Strategy

Marketing can cost your business money, so make sure that yours is actually effective. An article from Small Business Chronicle finds that in many cases, by reducing outside marketing and focusing instead on your customers you can cut costs without losing business. It's important to maintain some marketing presence, but taking a look at what you're currently spending vs. what it's actually bringing in might lead you to note that you're marketing is costing you more than the business it generates. In that case, it's probably time to switch up your strategies. To learn more about finding the right marketing path for your shop, check out our past blog, Selecting the Best Marketing Channels for Your Diesel Repair Shop.

Reduce Overhead Costs

Your overhead costs, or those expenses not directly associated with a repair sale, can take a large chunk out of your profits, especially if you're not careful. While some might believe that not much can be done to reduce overhead costs—it costs what it costs—that's not necessarily true. Even small adjustments can make a big impact on your overall profit. Review each cost and see if there is a way to reduce it.

Similarly, it's important to consider the growing overhead costs when growing your business. Yes, your overall goal is to increase sales and profitability, but oftentimes with those increases, there also comes a rise in your overhead costs. For example, if your sales volume increases, it's likely that your electricity usage will rise as well. This will be an added expense to consider as you work to increase sales. Planning for and managing those expenses can help you maintain or improve your net profit margin.

Why the Other Pieces are Important

So if the net profit margin tells you a lot about the profitability of your repair shop, you might be wondering why it's important that you continue to track the other metrics as well. Without looking at your gross profit margins, you're not getting the whole picture. By breaking it down, you can see how the individual parts make up your total profit. Is more money coming into your shop because of parts or labor? How much impact do your overhead costs have on the profits?
If you don't track all these metrics, you won't really be able to answer these questions and it will be harder for you to make a plan that targets how your shop is going to make more money. But, by monitoring all these profit margins, you have that information readily available to you, helping you to pinpoint the best strategies for your business.

EVALUATING YOUR POSTED LABOR RATE

Now we're taking a look at a metric you're almost certainly aware of, but you might not think about the actual impact it has on your profits—your posted labor rate. This number represents the amount per hour you charge your customers got for the work done on their vehicles. This is not the same as what your technicians are paid, as the goal should be to make money from your labor rate. Many shops aim for earning at least 50%.

It might sound straight forward enough, but it's still an important number to be familiar with and evaluate because of the impact it has on your bottom line—an impact that should be positive, but can be harmful if you're not careful and vigilant.

Deciding on Your Posted Labor Rate

When setting the labor rate for your shop, you need to make sure you're charging enough so that you're actually making money, not losing it. Because of this, you should evaluate the following numbers before deciding on your posted labor rate.

Technicians' Pay

The rate you charge your customer needs to be more than you're technicians cost you an hour, or you'll never be able to make money selling labor.

Technicians' Benefits

Along with their paycheck, you're also likely providing your technicians with benefits, like insurance, uniforms, tool allowances, etc. This is a cost to your business and should be taken into account when deciding on your posted labor rate.

Service/Parts Manager Salary and Benefits

While probably not actually turning wrenches, your service and/or parts manager is someone whose labor your pay for, and someone whom your customers benefit from. They should be paying for this expertise as part of the overall labor cost. Make sure you're considering this expense as you decide on your labor rate.

Overhead Costs

Just having your business open costs you money. From electric bills to insurance and taxes,there are things that will cost you money unassociated with any job order. You have to find a way to cover

these costs, and incorporating them into your labor rate can help ensure you have the money you need when the bills come in. Figure how much your shop spends on overhead costs. Include your salary, as well as any office staff, in these overhead costs.

Downtime

Inevitably, there will be times when your technicians aren't working on vehicles or your shop will have a slow period. Unfortunately, during these times you'll still need to sign paychecks and pay bills, so you should think about charging enough to buffer through those times you might not have as much coming in. This is especially important if you know when your slow times tend to be, particularly if they are seasonal. That helps you to predict how much you'll need to charge the rest of the year to see you through.

These costs are all important to factor into your decision, as is the amount of profit you want to make on top of that. Just by evaluating these figures and how they can be covered by the labor rate, you stand a better chance of running a profitable shop.

Things to Watch Out For

When thinking about your posted labor rate, there are some dangerous habits people tend to have. Try to avoid them as you move to make your shop more profitable.

Obsessing Over the Competition

Many shops are more concerned with what their competitors are charging than what their shop needs. Try not to be so focused on having the lowest prices, especially if doing so will drive you out of business. It's important that your rates are competitive and at least in the range of the market in your area. If you're unable to charge a market rate, it might be good to re-evaluate your costs. What expenses are preventing you from being a competitive, profitable shop? Is there a way you can reduce these to help you charge a better labor rate? You can check out our past blog, **Managing Labor to Maximize Your Diesel Repair Shop Profits**, to learn how managing your labor can help save your shop money.

Flat Rate for All Jobs

Are you charging a flat rate for labor on all the jobs that come through your shop? If you are, you might be losing money. Think about your different technicians. Do they all perform the same jobs at the same pay rate? If not, it doesn't make sense to charge your customer the same rate for a complicated job only your most skilled, highest paid tech could perform as you would an oil change any tech could do. You'd be losing money on the tech's labor costs. Instead, consider varying the rates depending on the job at hand. You'll be able to make more money, and it's easier to explain to a customer that the labor cost is so high because of the complicated nature of the repair.

Public Perception

Unfortunately, as a repair shop owner, you're fighting against the idea the public has about shops that take advantage of their customers. The current perception of labor costs is that they are way too high because shops are just trying to bleed every last penny they can out of the work. This is not the reality of the situation, though.

Oftentimes, shops charge barely enough on labor to cover their costs, let alone make a profit. This is a difficult way to run a business. Instead, try

to explain to the customer why labor costs are so high. Let them know the skilled expertise of your technicians. Give them thorough estimates that tell them exactly what is wrong with their vehicle. Show them that you're not trying to gouge them, but providing them with a valuable service that, because it is done by your expert staff, will actually save them money in the long run because they won't have to return as often for the same problem. It is possible to fight the stigma, and for the survival of repair shops, it's an important thing to do.

All in all, evaluating your posted labor rate is an important step in boosting your shop's profits. It feeds directly into your bottom line, so it's important you don't let it hinder your shop's growth.

YOUR EFFECTIVE LABOR RATE

Now we're going to bring it back into your shop as we look at your effective labor rate.

What is an Effective Labor Rate?

This metric might be a more difficult concept to understand, but it's one of the most important to track—you learn not only how much money you're making from your customers, but where money is being left on the table. A better understanding of the effective labor rate can truly lead to increased profits for your shop.

In a nutshell, your effective labor rate tells you what you make from your customers for each hour billed. Or, thinking about it another way, how much your technicians are costing you vs. what they are bringing in. You can calculate your effective labor rate by dividing the total labor sales by the hours billed to customers:

As a 2014 article from Ratchet+Wrench says, you want your effective labor rate to be as close to 100% as possible. Essentially, then, for every hour you are paying your technicians' wages, you want to be able to bill that hour to a customer. In this way, you are not losing money paying your technicians, but rather allowing your customer to pay them for you.

While this sounds simple enough, the danger really lies in not tracking your effective labor rate. If you're not paying attention to it, it is easy to lose hours, whether that be from ineffective systems and procedures or faulty estimates. Every hour not charged to a customer is an hour that you pay for out of your profits, and if you aren't tracking these hours, there's no way for you to maximize your profits.

Improving Your Effective Labor Rate

To really increase overall shop profits, you not only want to track your effective labor rate, but actively work to improve it. There are several strategies you could employ to bring up your effective labor rate:

Improve Systems

Having defined systems and procedures are crucial to helping your business run at its smoothest and most efficient. Evaluate the systems you currently have in place. Are there steps that could be simplified to save time? If you don't have any systems set up in your shop, work on documenting those procedures so that every employee knows exactly what is expected of them. Not only will you notice an increase in productivity, but it should help boost your effective labor rate as well.

Improve Estimates

Accurate estimates are key to improving your effective labor rate. If you're not quoting the proper number of hours to your customers, then not only do you not make money on every hour worked over that estimate, but the technicians' pay comes right out of your profit. Work with your service advisors to ensure that the most thorough and accurate quotes are being provided.

Along with that, make sure that you're charging for diagnostic time. This can easily be one of the most time-consuming steps, but often shops only bill the customers a flat rate. If a diagnostic ends up taking several hours, you're losing money. Make sure you're charging the customer for the time it actually takes to complete the diagnostic on their vehicle.

Increase Staff Productivity

Making your staff more productive can help raise your effective labor rate. The more productive your technicians are, the more billable hours you end up having to sell. We'll talk more about shop productivity in another section.

Invest in New Equipment

Take a look at the equipment in your shop. Do your technicians actually have everything they need to be able to complete the jobs in the hours quoted? Sometimes a new piece of equipment

is what you need to improve overall efficiency. You might want to consider investing in improved technology to help your techs finish each job within the estimate—or perhaps even faster. It will cost you money up front, but the consistent return from your increased effective labor rate should make up for that initial loss.

Charge for Non-Routine Tasks

Sometimes during a job your technicians will encounter something that isn't part of the regular quoted work, but that they have to take care of in order to complete the repair. This can add time to the job, causing them to go over the quoted hours. If this is the case, don't be afraid to charge the customers for the time—it's not a failing on the part of any of your employees, but unforeseen circumstances that made the repair more complicated than it initially appeared. You shouldn't lose money on occasions like this.

Improve Efficiency

One frequently cited way to improve your effective labor rate is to improve your technicians' efficiency. If they can complete a job quoted at 4 hours in 3, then you have the opportunity to bill that extra hour. We'll dive deeper into efficiency in an upcoming post.

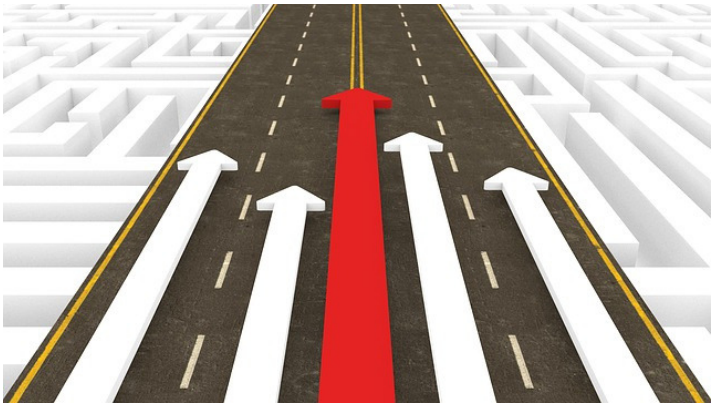
Things to Consider

That same Ratchet+Wrench article cautions against relying too heavily on efficiency as a tool to raise your effective labor rate. They find that even if your technicians are working faster, you still have to pay them for that time billed. You also have to be careful not to let increased efficiency lull you into a false sense of security. With a more efficient shop, you also gain the ability to sell more hours, but this is meaningless if you don't take advantage of it. Make sure that you're getting customers into your shop and filling the bays.

Fixed Magazine points to shop accountability in a June 2018 article as something else to think about as you work on your effective labor rate. It's one thing to say you want improved productivity and efficiency, but it's quite another to actually hold your staff accountable for it. It's something you need to foster in the environment of your shop. Your technicians need to feel valued and recognized for the hard work they put in. Keep your shop positive and the accountability should follow.

Like with most of the metrics discussed in this series, it takes active monitoring of the little things to make a big difference in your profits. But you'd be surprised at how quickly those smaller things add up.

AN EYE ON REPAIR SHOP PRODUCTIVITY



In an ideal world, everyone would be 100% productive all the time. Unfortunately, we're only human and haven't been able to achieve that goal. But that doesn't mean your shop can't be more productive than it currently is, just that you have to be very strategic about how you go about implementing changes to improve it.

What is Productivity?

Productivity as a metric is commonly thought of as a measurement of inputs and outputs—how much time and/or resources it takes to achieve the desired output.

Okay, so what does that mean for your shop? Productivity can be broken down into smaller pieces, namely overall shop productivity and individual technician productivity. Repair shop productivity can best be determined by dividing the number of technician hours available to be billed (most likely 8hrs/day multiplied by the number of technicians you have on staff) by the actual number of billable hours worked on a job.

This number allows you to better evaluate down-time and why it happens. Is there not enough work coming in? Ineffective processes? Trying to root cause this can help you decide on a way to improve.

Boosting Productivity

When you're looking at boosting productivity amongst your employees, the first thing that might come to your mind is that they'll want more money. Surprisingly, that's not the main thing on their mind. Think about some of these other ways to boost productivity that might make your employees happier in the long run and actually save your shop some money.

Ensure Proper Training and Equipment

It's hard to complete a job you haven't been trained to do, or without the necessary tools to do so. Evaluate what the environment is like in your shop. Are your technicians current on certifications? Are there trainings or refresher courses you could have them do that would not only make them more confident in their job, but make them more productive overall? This might cost you some money upfront, but the boost in morale and productivity should help regain those profits in no time.

It's the same with tools and equipment. Do your technicians have to use outdated resources to complete jobs? Updating the technology in your shop can help them complete their jobs more quickly and easily, increasing the number of hours available to sell to customers.

Work on Definite or Improved Standards and Processes

Do you have set processes in places to ensure everyone is completing jobs up to the standard of your shop and working as efficiently as possible? If so, make sure these processes are actually working as intended. Evaluate them for flaws or possible work stoppages. Try to see where improvements can be made to save everyone time in the shop and prevent lost hours.

If you don't have standards in place, it might be a good time to do so. It would better help you track how everyone's time should be spent, as well as more easily locate and resolve any issues that might arise. You'd be surprised to see overall productivity increase as well, as your employees can be more sure of exactly what is expected of them and act with confidence.

Rethink Shop Organization

Think about how your shop is currently set up. Is there a logical flow? Are your technicians easily able to locate and use the tools they need? Try to identify places where work might be slowed due to poor layout and see if there is way to reorganize. Aim to improve your technicians' ability to continue working without interruptions to go find a tool or part.

Evaluate Lost Time

Try to identify where time is getting lost in the shop. Is it because of the previously mentioned disorganization (either in processes or shop layout), or does it have to do with poor estimates? Make sure that your service manager and technicians are on the same page with estimates and what is expected of them. It's vital that the estimate given to the customer is accurate and achievable by your technicians, or you will be losing both time and money.

Decrease Downtime

Decreasing downtime comes down to how work is organized in your shop. Again, make sure that everyone in the shop is on the same page (this is where processes come in handy). Try to make sure that the right technicians are being assigned jobs and that you're not underutilizing your more skilled techs.

Work to Prevent Employee Turnover

As you may know, employee turnover costs your shop a lot of money. But even more than that, it stalls your productivity. Not only did you lose a skilled employee with the experience to get the job done, odds are you have to hire someone who will require training to get them to that level. That takes time and money, and assumes that you're able to find a replacement rapidly. You don't want to lose business simply because you don't have enough techs to do the work.

On average, employee turnover costs can be as much as $12,000 to $20,000 per employee.That's a lot of money for something you can work to prevent. Think about employing these strategies to help retain employees:

- Foster an environment that promotes and rewards excellence
-Redefine the value of your entry level employees
-Provide a work/life balance
-Listen to and encourage employee input
-Give your employees feedback on their performance, especially when they are doing well

Get Jobs Into Your Shop

It's impossible for your technicians to be productive if there are no vehicles for them to work on. Make sure that you're doing everything you can to ensure that your bays are filled. Work on establishing good customer relationships for repeat business. Develop a clear marketing strategy to drive in new business. If you want your technicians to do their job, you have to make sure there are jobs for them to do.

Some Things to Note

In their June 2018 issue, Ratchet+Wrench find that productivity is a metric most people are familiar with, but few know how to track. They note that by learning what productivity really is and tracking it in relation to other KPIs (key performance indicators), particularly effective labor rate, you can better identify benchmarks for productivity and increased profitability.

Tracking productivity is a good way to track trends in your business and it provides you with a better way to plan for the future. It does not, however, reveal the whole story. Remember that while productivity can be tied to profit, it does not tell you how profitable your shop actually is. That's why it's important to track multiple metrics to have the clearest idea of what's happening in you shop as a whole.

INCREASING EFFICIENCY, GROWING PROFIT

What is Efficiency?

Efficiency and productivity are closely linked, but efficiency looks specifically at the hours it actually takes a technician to complete a job vs. how much time the repair was estimated to be completed in.

Tracking efficiency can let you know how effective your shop is. It can also help you identify areas for improvement that can increase some of your other metrics as well. For example, increases in efficiency—particularly systems and workflow—can have a positive impact on your effective labor rate. This in turn directly impacts your bottom line.

Like productivity, efficiency can be looked at on the more global shop level, or on the individual technician level. Many shops aim to have their

efficiency rate at 100% or greater, which would then allow them more billable hours, and in turn higher profits. You can calculate your efficiency by dividing the hours billed by the actual number of hours your technicians took to complete the job and multiplying by 100:

What Can be Done to Improve Efficiency?

Just knowing what efficiency is doesn't do your shop a whole lot of good. The more important information is knowing how to improve it. Here are a few strategies you might employ to increase your shop's efficiency:

Improved Estimates and Communication

One of the main things you can do to improve your efficiency is to ensure that the estimates given to customers are as accurate as possible. If customers aren't quoted a realistic timeframe, your technicians are being set up for failure right from the start. Make sure that you have open lines of communication from the front and back of your shop to help ensure that each estimate is thorough and correct both before it is given to the customer, as well as throughout the repair process.

Scheduling

Scheduling for maximum efficiency doesn't mean pushing your technicians to their physical limits, but rather knowing your capacity and scheduling for it. Make sure you know the maximum number of billable hours your technicians are capable of (more experienced master techs can usually handle more than 8 billable hours, while an apprentice might only be able to handle 6 or 7). This will help you utilize each tech to their fullest. Schedule each repair to the technician best suited for it so that each person's time is spent in the most efficient way possible.

Bringing in Work

To be truly efficient, you have to make sure you're bringing work in to your shop. If your bays aren't full, you're not making money. But even more than that, you want to make sure you're bringing in the right work. Ratchet+Wrench's March 2014 **article** details this idea. They find that it's important for your business to be able to close sales on jobs that don't waste your technicians' time—partial jobs or unprofitable ones. With these jobs, it's difficult for your technicians to work faster than the hours booked and their efficiency really takes a hit. It helps, they go on, if you can sell a complete estimate, rather than a customer picking and choosing repairs.

Workflow

If you don't already have workflow processes in place, it would be a good idea to do so. This will help each of your employees know exactly what they should be doing, as well as what each person is responsible for. Having a set system of steps for jobs can also show you where time is being lost or wasted, and allow you to make improvements to the systems for overall increased efficiency. If you already have workflow systems, evaluate them. Are they still

working for your shop? Are there places they could be simplified or duties shifted to reduce the burden on one person?

Training and Equipment

One simple way to boost your efficiency is to make sure that your technicians have the training and equipment they need to complete their jobs. Rather than have your techs struggle on a job they don't have the proper tools for, invest in those specialty tools that will save you money in the long run. Allowing your techs access to continuing training will not only make them more knowledgeable, but they will be able to work faster because they'll be more confident in what they're doing.

Logical Shop Flow

This might seem like a given, but make sure that your shop is as organized as possible. Each tool should have its place and everyone should know where everything belongs. Lay out the shop as logically as possible so that time is not lost trying to locate something, or having to move large items from far away. Try to reduce garbage and clutter by throwing out old or unnecessary parts. Keep workbenches organized and tidy. This will reduce the amount of time lost because tools or parts can't be located, adding up to increased efficiency and profits.

Parts Availability

If you don't have the necessary parts readily available, you lose time on repairs, which loses you money. Try to ship complete orders so that you aren't stuck waiting for one thing to show up before you can continue your work. HHP offers fast shipping—2-days or less to most areas!

Some Things for Consideration

In order to truly foster an environment of efficiency, you need to make sure your employees understand why you're doing it, otherwise they're less likely to follow the systems. Let them know how their efficiency impacts the shop overall, as well as themselves directly. Consider offering incentives to keep them motivated. Keeping your shop a positive environment to work can also help motivate your employees.

Working faster alone will not make you more money. You need to be efficient in the right ways and be targeted about your approach. This is where the other metrics we've discussed in this series come in. Each one can help point your shop in the right overall direction.

As you begin to emphasize efficiency in your shop, make sure you don't sacrifice quality. Working more efficiently doesn't matter if you have a lot of customers return with issues on their repairs due to sloppy work. Make sure that quality work is seen as just as important as fast work.

Throughout the Profit Boosting Boot Camp series, we've taken a look at the different metrics you could track to help improve your overall profits. Taken individually, you get a small part of the picture, and might see some increased profits, but together is where their power truly lies. They feed into each other. By implementing this monitoring in your shop, you can not only see where money-making opportunities are, you can make a plan to actively work towards achieving your future goals for your shop.

Another way to improve your profits is by saving money on parts. Check out our Repair Shop Value program to see how our great benefits could save your shop money. Learn more **here**.