Size Matters

The concept that size doesn't matter has been proven incorrect in almost every application where those without try to claim a level of parity to those with. In many cases, the differential between those with size and those without can be minimized. Business is not one of them.

Certainly there are areas of business where smaller companies can compete. Over the years Tudog has been in the forefront of assisting small companies to effectively compete against larger ones. But the issue of size and the benefits it affords makes the task of competing one that requires focus on the weaknesses of larger companies. Size matters when it comes to their strengths.

The primary strength of a large company is its ability to leverage the concept of economies of scale, which means that as the company grows and produces more, it is able to acquire the components of its product (or service) for less per unit, thereby effectively lowering the cost of each unit sold. Depending on the market, this ability to produce each unit at a lower cost can allow the company to either go to market at a price lower than its competitions, or extract higher profit from each unit sold.

The benefits of economies of scale are not exclusively the domain of larger companies, even though their chances of reaching the critical mass needed to execute are greater. For smaller companies, the better the understanding of economies of scale, the better the chances of finding a way to exploit the principle. To assist in this understanding, Tudog has identified 3 circumstances under which economies of scale are likely to occur. They are:

1. Maximization of Production

Any production capacity that is not being utilized is a waste of capacity and could be limiting the economies of scales. There are two ways to make sure your company does not have excess capacity; you can either sell any unused capacity you may have to other companies that need to produce what you produce, or you can construct your production capabilities in such a way (lean manufacturing) so as to expand capacity as demand requires (limiting the excess capacity).

By using all the capacity created, the company should be able to adopt some degree of economies of scale, leading to operational efficiencies and a reduction in cost per unit construction.

2. Specialization

The accumulation of volume could allow your company to begin to assign specific and concentrated tasks to both its machines and manpower. By doing this it allows the dedicated machines to work without the need for adjustment (to new tasks) and with efficiencies that continual operations enables. By assigning staff to consistent tasks, you are allowing them to grow highly proficient and acquire skills through practice (and repetition) that enable them to perform at higher levels of productivity and quality.

By engaging in specialization, you are creating an opportunity for the impact of economies of scale to take effect. This will serve to benefit the company, as additional efficiencies and higher quality levels in turn drive higher sales.

Smaller companies can begin to position themselves to gain the advantages of specialization by moving away from the tendency to use all employees for all tasks and allow for some to be assigned to permanent tasks at which they can grow skillful. By doing this, the output cost could remain stable and the unit costs should ultimately fall.

3. Increased Buying Power

The more you buy the stronger your negotiating position becomes as your suppliers recognize the need to adjust pricing in order to maintain your growing business. This in turn leads to your ability to lower prices to your customers, which will in turn influence your volume (enlarging it). The effect is then cascading, as the increased volume leads to more orders by you, which in turn makes you more valuable to your suppliers, so they maintain low prices.

Economies of Scale is useful not only because it can lead to a dramatic reduction in cost, which if passed on even partially to customers, can also result in a dramatic increase in sales, but also because in many cases it can create a necessary barrier of entry that serves to limit competitive pressures. As a company enhances its economies of scale, its capabilities to deliver quality at lower prices forces competitors to make operational adjustments and cautions potential competitors regarding the viability of their entry.

In creating economies of scale you can get in your own way if you don't handle your growth properly. You need to make sure that as you grow the systems you put into place maintain the integrity of the efficiencies you are seeking to create and safeguard. You need to be sure you don't lose the advantages by eating up additional costs as you expand.

Also, there are many companies that find a sharp increase in their transactional costs as they fail to take into account distribution and logistical expenses that could increase as you implement a centralized system. You need to make sure you go through the proper analysis process to determine the costs and benefits to your campaign, making sure that the savings you anticipate actually occur and that you're able to transfer at least a portion of them to your customers.

Finally, many companies lose in bureaucracy what they gained in economies of scale because they increase their processes as they increase operations, even creating duplications of task along the way. This is not entirely necessary, even though you may need to expand out a bit to maintain quality.

Even small companies should strive to attain some level of economies of scale. The benefits outweigh the risks and costs, and help the small players reduce the truth behind the statement, size matters.