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Growing Your Business ORGANICALLY

THE RULE OF 350

by Rodman Heckman

In the past eighteen months, several prominent party plan companies closed their doors, despite having pre-established brand equity and strong financial support from a successful corporate parent. Was there a common factor? Is there an inherent problem with introducing retail brands to the party plan channel? Or are we perhaps applying the wrong standard for success?

Experience teaches us that a number of variables can prevent a party plan business from reaching its full potential. Among the most important are the following:

- Recruiting and retention
- Salesforce activity and productivity
- Product appeal
- Repeatable model
- Ease of doing business

The introduction of outside investors, however, adds another variable—a quest for rapid growth. Successful investors and successful consumer brands approach the direct selling channel with an impatience and aggressiveness that has served them well in the traditional retail channel. It's in their DNA.

And sometimes they succeed. Southern Living At Home set the bar very high when they enrolled 25,000 consultants within two years of their launch. That extraordinary accomplishment has influenced every corporate parent that followed.

The Case for Organic Growth

In party plan, however, organic growth—particularly in Year One—is usually a better formula for long-term success. The ideal is to grow organically, primarily by recruiting at parties, and to support the new recruits in person through leader-led training and motivation. It is an industry axiom that those consultants enrolled through the party process are more productive and remain active longer. Face-to-face training and motivation—offered one-on-one and at leader-led monthly meetings—are the warp and weft of the party plan fabric. It is what creates the company culture. It is what allows party plan companies to enjoy the scale and longevity they do.

Organic growth, driven by local recruiting and nurtured by monthly leader meetings, is smart growth. Sustainable growth. And you can demonstrate it using simple financial modeling.

The Rule of 350

Let's say you are a start-up company building a five-year financial plan. Many of the assumptions about revenue and expenses will necessarily vary by category and company. But surprisingly, the most significant driver—salesforce growth—follows a very consistent pattern from company to company.

In fact, if you have just 350 enrolled consultants, and if you manage your recruiting and retention to industry standards, you can contemplate the possibility of being a $100 million business within five years.

Are you skeptical? You can prove this for yourself using an electronic spreadsheet:

1. Begin with 20 Consultants. (Anything less than that is a Pilot Program.)
2. Set your projected activity rate. Let's say that *active* means the consultant turned in one party during the month, and let's use 55 percent as a reasonable assumption—slightly more than half your enrolled base is active in any given month. Activity rate will rise and fall dramatically month-by-month, but the annual average will be 55 percent.
3. Now plug in a recruiting rate as a percentage of your active consultants. Start slowly, and ramp it up to 20 percent. That's typical of industry best practice.
4. As the size of the salesforce grows, drop the recruiting rate year-by-year. Our model drops to just 8 percent in Year Five. Again, conservative.

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5. Now, let's build in attrition. We have used 40 percent. That assumes that almost everyone who was inactive does not renew at their anniversary. A few re-enroll even though they did not meet our definition of active; they are in effect a buyer's club.
6. If you agree that the assumptions are reasonable, and we would argue that they are, based on years of experience with scores of companies, the consultant count grows as follows:

End of Year One:	350	Consultants
End of Year Two:	1,600	Consultants
End of Year Three:	4,400	Consultants
End of Year Four:	9,000	Consultants
End of Year Five:	20,000	Consultants

7. While revenue will vary, we can roughly translate the consultant count to dollars as follows:

- 20,000 consultants in Year Five will generate 144,000 parties.
- A $46 average customer order grosses up to a $560 party, when you include Hostess Awards at suggested retail price.
- That's $83 million in party gross revenue alone, before starter kits, sales aids and nonparty sales.
- In total, $98 million in gross (retail) revenue.

Now, let's assume that your results differ from the model for some reason, and you miss by half. You should still be planning for the possibility of a $50 million business in Year Five.

Are you still skeptical? Consider a few real-life examples:

- Tastefully Simple had 350 enrolled consultants in 1999. Five years later, the company had 20,000 enrolled consultants and revenue of $120 million.
- Creative Memories enrolled consultant No. 350 in 1990. Six years later, they had 22,000 consultants, and their consultant count has tripled since then to almost 70,000.

Organic Growth vs. the Need for Speed

When you are undertaking a party plan start-up, whether it is new or with pre-established brand equity from another channel, there are three problems with fast growth.

- It is difficult to accomplish. As a cautionary tale, consider that last fall a major apparel retailer closed its party plan division. In our view, management did an excellent job in product design, brand positioning and the development of marketing materials. We believe it would have been a successful party plan company, and recruiting was tracking well ahead of the Rule of 350. But the budget called for very aggressive recruiting in Year One and, despite some very creative recruiting programs, the company failed to meet expectations.
- Even if you achieve the recruiting numbers, the performance of the recruits will suffer. Under any circumstances, it is difficult to train a large number of people in a compressed period. When the company is young, and the staffing and infrastructure are still forming, it is considerably more difficult. In fall 2005, a major cataloger closed its party plan division despite the fact that the company had recruited almost 2,500 consultants within one year of its launch. The party plan division successfully leveraged the parent's name to accelerate enrollment, but activity levels were suppressed. Recruits enrolled, but didn't engage. Were they just "kit-nappers" who joined only to get the products in the Starter Kit at a discounted price? We would argue that they joined with the best intentions, but the rapid growth process lacked the integrity and support that are inherent in organic growth. The enrollment numbers were fallacious—misleading.
- The problem is compounded by geography. Rapid recruiting typically involves Internet advertising and remote enrollment. As a result, you find that you have enrolled recruits in Michigan, Montana, Minnesota, Maryland and Maine, and it is very challenging to instill the leader-led training and motivation that comes inherently with organic growth.

What is the Downside to Organic Growth?

Clearly, organic growth has a downside. Organic growth means slower revenue ramp-up and a theoretical delay in reaching break-even. This must be factored into the investment strategy. A financial budget based on rapid Year One growth seems to solve problems, particularly with cumulative out-of-pocket expenses and cash flow. But our point is that *it is actually increasing risk, not diminishing it,* because the salesforce assumptions are fallacious. You can build the aggressive numbers into the plan, but it doesn't mean you will achieve them.

Additionally, as the numbers demonstrate, growth in later years can be expected to be exponential once the stronger, organic foundation is established.

Where Do We Go from Here?

It takes plenty of courage—and a lot of supporting evidence—to say no to rapid early growth. It is very difficult politically both for the corporate parent and for those on the operating team who have direct selling expertise.

But direct selling is not the same as traditional retail. It has its own needs and drivers, and we need to understand and explain how to appropriately measure success in this industry. We are doing a grave disservice to our investors and our partners from other channels when we abdicate our responsibility to speak up and say no to rapid early growth.

Organic growth in Year One means more time for management to focus on the other key factors—like retention, activity, communication and training. More time to focus on ensuring that every detail of operations contributes to a fun, easy business. More time to fine-tune the repeatable model.

Let's not put long-term success at risk for the sake of rapid early growth. Consider the Rule of 350.

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