The Business Review of the Eric Rosenquist Institution

Draft – Confidential

RUNAWAY PROFITS

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It is not inconceivable, nor out of reach. Our staid planning has it as an idealized goal, perhaps never conceived as realistic, laughed off. When it comes, it is astonishing, but signals the end of astonishment–if dealt with cautiously.

I speak of course of runaway profits. Some of us, if we are lucky (or unlucky) enough to know a situation where the profits exponentially exceed our expectations, will live a life only dreamed of–for a while. These days, the exponent is 500, the expectations humble, modern, bold, and maybe decadent. But the profits can quickly take hold and, like the wings of Icarus, melt away above a sea of enraged investors.

In Icarus, find we flight, beg fatherhood;
In debt, find credit, exaltation, fame;
In fell precipitation, fall from flame;
In cavern hides thy kingdom vile or good
–R. *Flemton Howell, cell wall inscription*

Break them down any way you want, long-term, short-term, fixed, variable, shared, compensated, estimated, contingent, they are increasing without an end in sight. Everyone knows it; conversations in the office have taken a decidedly optimistic bent. Some might have an idea of how it happened, but this is irrelevant now. A textbook analysis might keep grounded the temptation to forget why it went right this time, in the moment, but the textbooks lie at home. There are no textbooks here.

Someone, most likely the most sober and senior, will start to fear the future. The force of complacency will be a formidable foe, and a true leader will defeat it with skill and tact.

Runaway profits are the ultimate goal and ultimately the downfall, like a child's coveted toy a disappointment after a short two weeks. The two weeks might come in the form of two years, two months, two hours. Something should smell foul in the forest, overlooked for the trees. The profits come from the rich, make the poor richer–until the day the rich are uprooted as the French nobility, the source dries up. And a confrontational approach might be taken, albeit reluctantly: why are the profits so high? Why are expenditures so *low*? Like a new boat, the profits will be the envy of all the neighbors, and they will move in quickly next door. The only thing that will be running away at that point is the number of competitors, and perhaps yourself.

WHAT THIS IS NOT

The second cousin of runaway profits, runaway revenues, has been blamed for the dot-com "bust" of recent quarters–with mixed merit (see T.F. Bohut's 1998 forecast, apt to our dying day). This facile scapegoating is, ironically, rooted in the lack of accompanying runaway profits. In a seeming direct contravention of these "logics," runaway investment, prized by all parties involved, may easily continue indefinitely, *even in the absence of profits*. The upward limitation is the size of the world economy, unattainable trillions. In practice, lack of confidence, frivolous fears, and a bandwagon trend model are the ultimate demise of a company. This outcome may be considered inconclusive.

THEORY

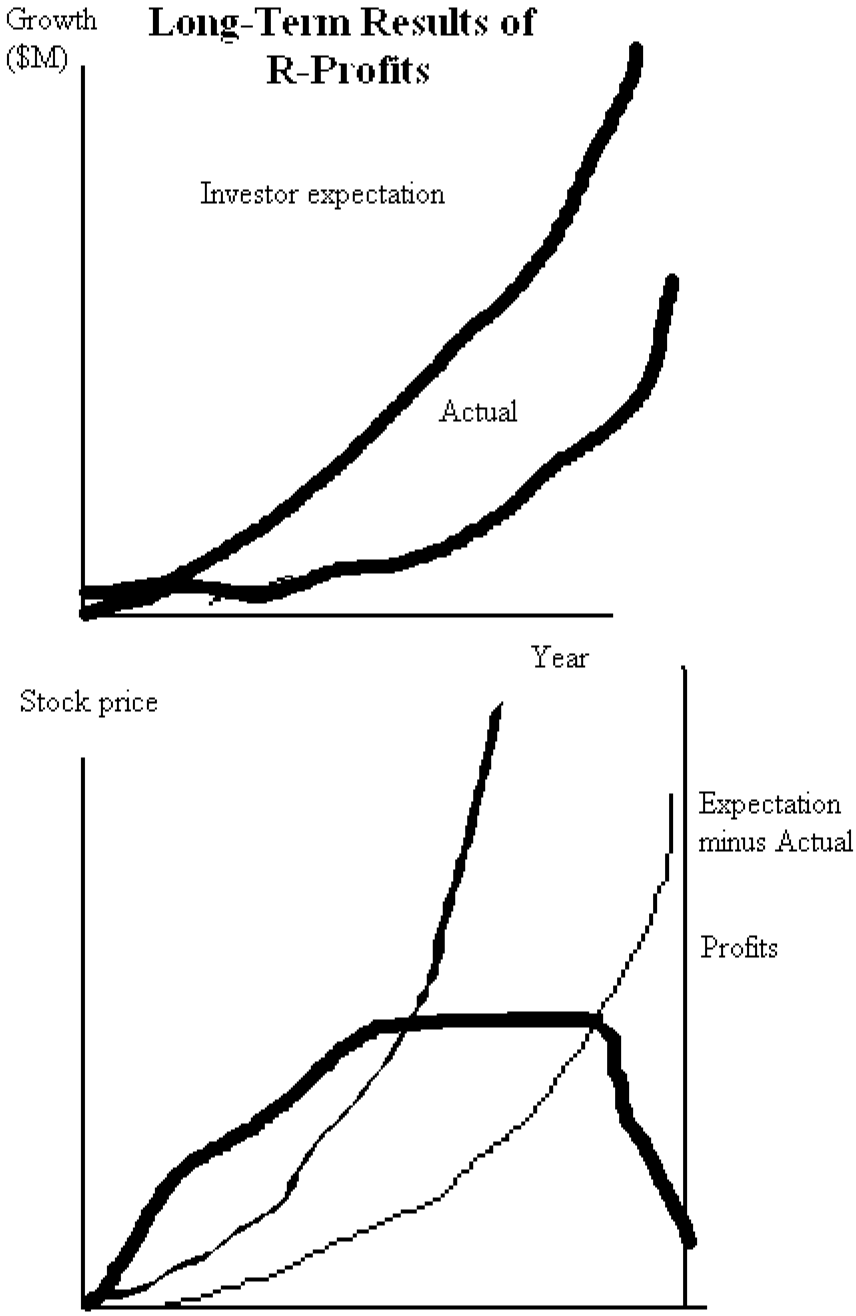
In theory, runaway profits could continue forever, again limited only by the trillion-gargantua of the trusted "world economy." Even with a reduction to a market-centric analytical space, market forecasts may grow to infinity, and a company already posting runaway profits is poised for an optimistic *indefinity estimation* (see Bohut 1994) –its bounds may assessed solely on the basis of current conditions. Additionally, extrapolative analysis based on past double-exponential, exponential, or linear upward trends with a base of 1.01 or greater remains at the forefront of sober risk-logarithmic standard practice.

Having added calculation to informal office mood and intuition, we might conclude that runaway profits are unassailable, and some would argue that this inchoate formulation adequately characterizes under all parameter stresses. The issue might easily be dismissed with the observation that runaway expenditures could meet or exceed profit overshoots, keeping in check the profit-to-earnings or earnings-to-profit ratio. However, expenditures *diminish* the effects of the profits, masking the true threat.

MODEL

At the critical juncture, a reasoning model must be chosen that encompasses human factors, a favorable portfolio of unemployment-availability indices, risk-logarithmic stipulation, and accounting deferment maximization. Previously feared as a destabilizing influence on investor opinion, such models might only be easily defensible in light of five-nines irregularities, worth not the paper they are written on times 0.00001.

Chief among the threats from the r-profit curve is the instablity even under short term intervals. The instability comes in three forms: investor expectation logarithm, internal production cost bloat factor, and sub-model cash supply. Of these, the third has proved in documented cases to be the greatest, and the most inexplicable, single factor cited.


Growth
($M)
Long-Term Results of
R-Profits
Investor expectation
Actual
Year
Stock price
Expectation
minus Actual
Profits
Year

REMEDIES

The approach most likely to sit well with investors is investment of the profits to expand the company. However, it is crucial that these investments not be haphazard. A portfolio must be culled from stocks related and unrelated fields, particularly including competitors on a direct level and on higher levels such as distributors, marketers, and retailers (as applicable). Substantial public investment in such interests should be followed by a timed selloff of own stock. The effect causality of this scheme is not absolute or direct, but its success potential relative to the risk comes in a necessarily high ratio if properly executed. The risks concern uncertainty in the factors of revenue depression and cost inflation. If not properly hedged, the investments may succeed or fail outside their anticipated ranges. A profit growth situation in this case may in fact be escalated. Particularly in the case for example of distributors with no long-term fixed interests, investment may shape the course of their future decisions in one's favor.

Reduction of prices and increases of bond interest rates both directly influence the income-payout metric and may seem favorable, but the altogether uncertain danger is a disproportionate shift of the market toward these improved offerings. In the case of substantial market influence, this increase may be stabilized and even reversed depending on fierce price competition. Ipso facto, success is not assured through crude attempts at market maniplation. In more complex manipulation regimes, adaptive to market shifts, the reduction may be achieved with greater stability and direction under a conducive market share profile.

In the 1990s the major push was to increase productivity, driving down total wage growth, time-to-market, R&D budgets, and employment indices. It runs counter to this trend to reduce productivity in the interest of curbing profits, but aside from its bitter necessity it almost inevitably brings side benefits, often of a great magnitude. "Modernized" equipment, latest-generation software, the much ballyhooed cassette-based employee modification regimes, leather planners, personal digital assistants–the list goes continues of cost saving potential. Though it appears to increase profits again, this reduction takes the form of an "inverse-spend-to-yield" tradeoff as discussed in more detail in W.D. Bohut's *The Art of Business War* (1994): its impact *after* the profit increase is necessarily of a greater magnitude.

CONCLUSION

We all wish for one thing–or we wish for a few things, but this is the clincher. Our blood sweat and tears go daily to this grind, this quest consumes our attention, our personal lives, our weekends; in short, our livelihood *is* profits. Should a situation arise with unbounded excess over expectation, temporally and quantitatively, the limits of known models are tested, with caution as their bottom line.

Though it is claimed in the passionate boardroom that no curve can capture the essence of a leadership team, nor the essence of the bottom line, these curve models should serve as an Aristotelian sobering during an ill-timed celebration.

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consulting firm specializing in mathematical and statistical forecasting. His recent tempering of runaway profits for several major clients was widely recognized as an application of cutting-edge research with real-world consequences.