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Death benefits

The funeral sector offers many possibilities for growth, but the emotional barriers to reinventing the industry must be overcome, explains Tony Grundy

MBA thinking can be applied just as well to more mature markets as to new and fast-growing sectors. In traditional corporate planning, truly attractive industries are thought to be those that are, or are about to become, high growth. But growth potential can also be latent.

For instance, before the early 2000s it was felt that the healthclub market had expanded as far as possible – until Matthew Harris, CEO of FitnessforLess, saw budget gyms as a growth sector (see previous article, December 2014).

One industry with hidden potential is the funeral sector. Between 1980 and 2000, the funeral care market actually grew in the UK, with the average spend going up in real terms. Families were prepared to spend more on this product of considerable emotional value. The value of estates grew too. In addition, not only was more spent, on average, on the whole funeral process; spending on the core product also went up – the services associated with the 'disposal' itself (including a reported increase in embalming).

The actual market size has thus increased, even though demographics have reduced the death rate in the UK. So sales growth rate as a key driver of economic value has been very positive. Who would have thought of the funerals market as a growth sector?

Value creation in a given industry is driven by the existence or otherwise of 'competitive pressure'. This is critical in determining the second key driver of economic value: operating profit margin, or return on sales. Competitive pressure here means:

* buyer power: very low
* supplier power: moderate
* competitive rivalry: low
* substitutes: extremely low
* entry barriers: see below.

Entry barriers vary: although the economic entry barriers are not that huge, the psychological ones are actually very high indeed, as dealing with corpses seems to carry with it a certain stigma. The funeral director is arguably a less appealing type of finance director.

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Ripe for the picking

Looking at the five aspects of competitive pressure listed above (sometimes known as Porter's five forces), you would have to conclude that this is a rather attractive industry – indeed, as no force is actually negative, it is a 'five-star' industry. Such industries are characterised by high returns on net assets and stong economic value creation. And this gets better where there is some market growth.

Indeed it is not impossible to achieve net profit as a percentage of sales nearing 20%. The industry is also relatively free of regulatory pressures that might push up costs and squeeze margins. However, on the flip side, that does mean lower regulatory barriers to entry, leaving the industry structure potentially vulnerable.

This means that the industry is similar in many ways to the weddings business, some areas of pharmaceuticals such as the IVF market, the adult electronic gaming industry, and others where there are strong buying habits (maybe even quasi-addictive ones). All of these markets exhibit more naturally easy ways of making money than those one, two and three-star industries that economists would describe as 'partly or fully commoditised'.

Not only are the forces of competitive pressure crucial determinants of profitability and return, but these industry structures and dynamics are ones that can be reshaped.

For example, in a classic UK television documentary some years ago, former undertaker and entrepreneur Howard Hodgson told of how he led the transformation of the industry through a combination of acquisition, consolidation, value innovation and cost management. In his book *How To Become Dead Rich* Hodgson set out his vision of how to to run his funeral business as economically as possible, with an efficient set of local operations providing up to several funerals in a day, making much better use of facilities such as cars, storage and sales facilities. Alongside this he pioneered a more extensive range of services, optimising the average price.

Remembering the dead

The Ancient Egyptians used death masks to guard the soul from evil spirits. Today's death rituals may be less elaborate, but funeral care is a growth market

This hugely widened operating profit margin and increased return on net assets.

This vision became the model of the Great Southern Group, which Hodgson sold out to and which, after a period of being owned by US company Service Corporation International, is now called Dignity, one of the UK's top players. These changes also reduced competitive rivalry in the UK market, where a higher proportion of the market had previously been fragmented, made up of 'mom and pop' independents.

The final frontier

After book retailing (Amazon), vacuum cleaners (Dyson) and toilets – virtually unchanged for 200 years – funerals could be regarded as a final frontier for innovation and reinvention. A single new player could potentially create a new submarket that could ultimately rival the existing industry paradigm.

There are many ways that one could innovate in this industry: pre-need funerals (where people plan their own funerals) are one example of a big opportunity in the UK, but they require overcoming emotional resistance – often the key to unlocking growth.

Issues that might keep a CEO of a funerals company awake at night might include:

* What could precipitate a major fall in margins in the industry?
* What kind of new entrant into the industry should we be worried about?
* How can I get the board to think seriously about the future when there has been such stability for so long?
* Could we sell funerals as a set of emotional needs and experiences that encompasses pre-need, event organisation and follow-on services, including grief support and therapy?
* If I were an alien entering the industry, what would I do differently? ■

Dr Tony Grundy is an independent consultant and trainer, and lectures at Henley Business School

For more information:

www.tonygrundy.com

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