Categories
U.S. news
World news
Politics
Business
Stocks & economy
U.S. business
World business
Autos
Real estate
Retail
Careers
Money
Small business
Viewpoints
Sports
Entertainment
Health
Tech & science
Travel

Time-tested businesses that still rake it in

You can make a decent living making recordings ... or soap


Wanna rock? Sound recording studios clock a 13 percent average pretax margin.

By Maureen Farrell
updated 4:13 p.m. ET, Fri., Feb. 29, 2008

Tech titans like Microsoft, Google and Yahoo! grab headlines, but there are a slew of traditional, targeted businesses that yield big profits for small players.

With the help of Sageworks, a Raleigh, N.C.-based private-company data provider, Forbes.com has identified 10 time-tested, comfortably profitable businesses — on a pretax basis — that aspiring entrepreneurs might hope to launch. While based on U.S. companies, the data also shed light on global profit trends.

The figures were drawn from the past eight years' worth of financial statements (nearly an entire business cycle) from several hundred thousand privately held companies in the U.S. — most with annual revenues under $10 million — and bucketed by Internal Revenue Service classifications.

Average pretax profits ranged from 8 percent to 13 percent. We included only industries for which Sageworks had data from at least 50 companies and eliminated categories too broad to be meaningful. (One caveat: The data have an inherent survivorship bias, as some companies captured in earlier years may have failed along the way.)

These time-worn small businesses run the gamut — from mining services to poultry farming — and all owe their profitability, in great part, to mining a niche.

"In some industries, knowing an area, its people and its geography matters more than scale," says James Nolen, professor of finance at the University of Texas at Austin. "Smaller companies can also respond to changing industry dynamics [better] than their larger counterparts."

While some of these businesses are more cyclical and require greater upfront investment than others, all boast respectable operating margins over the eight-year period.

Take sound recording studios, which clock a 13 percent average pretax margin. Sound studios lie between aspiring artists and their dreams — a potentially lucrative spot in the value chain, for those who play it right. While the upfront investment in equipment can be steep, variable costs are manageable. Greater production capability (say, layering in multiple tracks) commands higher prices — as do connections with the record labels.

Other businesses generate high returns because of perceived switching costs. Example: metal mining services, with a 12.6 percent average pretax margin. Preparing sites for excavations, conducting vibration tests and performing a bevy of other mining-related services is profitable work, especially when commodity prices are on the rise. While initial equipment costs may be high, nab a few customers and they'll probably stick with you.

"High skill and reliability does command a premium," says J.K. Gilless, an economics professor at the University of California at Berkeley. "These industries also rely strongly on word-of-mouth. Good contractors do really well and get lots of work."

Laments about the shrinking U.S. manufacturing base notwithstanding, small shops that manage to make and market a basic chemical post a respectable 9.4 percent average pretax margin. While the costs to crank out everything from vitamins to soaps are relatively low, the price tags are high.

"There are niches everywhere here," says Nolen. "You can make soap for a restaurant. You can brand bromide as a natural pesticide to kill roaches." And because these manufacturers can circumvent the U.S. Food and Drug Administration, they can take products to market quickly and make bold claims.

Yet another profitable niche: infrastructure support. Maintaining railroads (cars and lines) is the work of many locally based contractors. These companies provide rail car and cargo storage, unloading services, and cleaning — and clock an 8.6 percent average operating margin along the way.

Freight rail companies have been busier than usual because higher fuel prices make rail transport a viable option versus trucks — good news for small service companies, notes Curt Grimm, professor of supply chain and strategy at the University of Maryland's Robert H. Smith School of Business. "There's no substitute for the services," he says. "The lack of competitive options for the big railroads translates into higher volumes and higher prices."

But you don't have to get your hands dirty to post a decent profit in a traditional business. Just look at "grant-making and giving" services, which yield an average 10.1 percent pretax margin.

Plenty of nonprofits outsource their fundraising efforts and event planning. Providers of these services, many of them small shops, tend to charge flat fees versus a percentage of funds raised. Overhead is low enough — a computer and a cellphone might do the trick — and once you have a proven track record, you can charge decent rates.