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You can offset inflation with reinvention

For those of you with a swimming pool, you'll remember the shortage of chlorine tablets this past spring as the result of a Louisiana factory fire. Prices for the tabs soared — if you could find them at all.

But run down the long list of other shortages — from takeout ketchup packets to computer chips, lumber, truck drivers, shipping containers, jet fuel, and even people to fill jobs — and you'll notice every other one was somehow pandemic-related. As were the subsequent price and wage increases.

This has the Federal Reserve and the White House intimating that the jump in inflation setting off alarm bells on Wall Street is probably temporary and will magically go way without any dire need for radical tightening of fiscal policy.

Business owners and investors shouldn't bank on that. Especially considering the White House has now more than doubled its annual inflation forecast from 2 percent to 4.8 in the fourth quarter. As supply chain disruptions continue to jack up prices, businesses should instead be looking at inflation as an opportunity to revisit their margins and how they reinvent their products and/or services.

If it turns out that some causes of inflation are indeed temporary, businesses could make themselves even more profitable when things subside, if they're proactive now.

Elastic or inelastic?

The first question that needs to be answered is whether the price you charge for your product or service is elastic or inelastic. In other words, is there a correlation between demand and price increases or decreases? For example, if the demand decreases because the price increased, then your pricing model is elastic.

For the consumer, coping with products that have price elasticity is mostly about finding substitutes. And necessity — versus a luxury — is a function of elasticity, too. You usually don't

have to pay top dollar for big-name brands of products, because there are many alternatives. Conversely, you're going to have to pay whatever is charged for a medical procedure if it is unique or has limited supply.

Like the medical procedure, prices on some things are inelastic, meaning people will pay more, regardless, for toilet paper, gasoline, food — and pool tabs. So, inelastic pricing somewhat insulates the company, but in either case, inflation is cause to look at your margins.

One reason is that, eventually, a competitor will find a way to deliver a product that, while a necessity, is cheaper or better than yours, and serves the same purpose. Because that competitor did their homework.

Can you buy materials from different sources that are cheaper? Can you substitute materials to control costs? Can you change manufacturing or delivery modes? How can labor costs be controlled?

And how are you affected by the death of just-in-time ordering? This happened in the U.K. when businesses feared Brexit supply chain disruption and started hoarding materials, and the pandemic shortages accelerated that reversal.

And what about labor? Does the business need local workers, or can they be anywhere? There was a time when, if a business relocated, they'd offer to relocate employees, too, but that's not always necessary now. In fact, people are often unwilling to move in this new labor environment.

Labor is, irrefutably, a key ingredient in the current rate of inflation, as companies pay more to attract and retain scarce qualified workers. And those are pay increases that are not going to be some temporary pandemic phenomenon.

Raising prices

Many businesses have already responded to inflation by raising prices, from burger chain Shake Shack to the maker of Dove soap, in an effort to swallow higher materials and shipping costs.

Of course, raising prices is a surefire way to find out if your pricing is elastic. But if it is, can you reposition your product so that the buyer is willing to pay more? Think of Rolodex. And in the earliest days of credit cards, Carte Blanche did that, with American Express following suit. You just might find that your customers are willing to pay more than you have been charging.

The big players out there are already changing the business landscape by reinventing themselves and taking advantage of changes in consumer habits that are very likely going to be permanent.

Ford is planning on circumventing its dealers by selling more cars from the factory, Walmart is setting up clinics with doctors, Amazon is planning brick-and-mortar department stores — after aggravating the shortage of truck drivers by hiring as many as they could — and Wendy's is planning 700 delivery-only ghost kitchens.

Even small businesses can capitalize on going through this exercise. But it takes some fortitude — and a lot of research — to take the risks you need to offset the effects of inflation and a changing marketplace. Not every experiment will prove a panacea. But you don't have to be first to revisit your margins and reinvent what you're selling.

You just have to make sure you're not last.

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