LEASING:
Easing the cash crunch

With working capital getting scarce, contractors may find leasing arrangements attractive

Maybe cash will be hard to come by in 1976.
And, then, maybe it will not.
But many wall and ceiling contractors are already experiencing enough difficulty in the working capital squeeze to prompt them to look around for other financing alternatives.
And there is a way to loosen the financing crunch and to liberate capital funds that might not otherwise be available.
It is through leasing equipment rather than buying or owning it outright. Many contractors have found that leasing, which is really a pay-as-you-use approach, can conserve capital so that the contractor’s funds may be put to more productive and profitable uses.

Conserves Capital
It allows a construction firm not only to conserve working capital but also borrowing capacity during these inflationary times when it is to the contractor’s advantage to keep sources of cash available. When money is tight, leasing represents an attractive option for the smaller contractor, especially, to obtain new equipment without jeopardizing his bank credit lines.
There is no doubt that outright purchase of capital equipment usually entails fewer dollars. But with inflation, it is becoming increasingly more difficult for a contractor to keep sufficient money in the till to run his business comfortably.
While the investment in the new equipment can be depreciated year after year this procedure still subtracts from capital funds, retained earnings, or working capital which might otherwise be used more gainfully by the company.
Borrowing to buy new equipment may also cost less in dollars than does leasing, but the down payment of perhaps 20 to 25 percent has to come out of capital, and the balance remains to be paid over a period of years.
When the principal amount is financed by a bank loan it has the effect of shortening the line of credit at the bank. Banks generally want a 10 to 20 percent compensatory deposit which adds an unseen but significant cost to the contractor who borrows to buy equipment.
While leasing has been recognized as one of the more expensive ways to financing anything, in a period of rising prices the regular payments are paid in cheapening dollars during the term of the lease.
The equipment lessor’s interest charge basis may be set at a floating rate which changes from month to month in order to conform with the commercial banking prime interest rate. Such a device as a floating, changeable rate is important because it prevents any lock-in at a fixed high interest cost for years.

Covers Several Years
At the same time, the equipment leasing company provides intermediate term financing which covers a several year span. Intermediate means that it is not short-term pay-out, such as with a commercial bank, nor is it long-term as, for example, a bond issue usually is.
Furthermore, a contractor who leases capital equipment is confined to the equipment only through the span of the lease, usually with an option to renew.
In any event, any leasing arrangement has to be tailored to meet a contractor’s specific needs, because sound management calls for flexibility so that unanticipated needs can be met.
With some leasing arrangements, a lessee may be able to trade-up or trade-down for different kinds of equipment if existing equipment no longer serves its purpose.

There are many companies engaged in the leasing of construction equipment. A contractor who considers a leasing arrangement should pursue a careful, investigation just as he might do with any other important investment.
The price tag on specialized construction equipment is sufficiently high that the time taken to investigate carefully can produce distinct advantages for a prudent contractor.

Following are some questions that every contractor should ask when considering a leasing arrangement:

**What is the lease’s true cost?** Some leasing companies offer a mere monthly payment quotation, but a contractor should find out the details about “hidden details” such as the possibility of front-end payments, the amount of residual value, administrative fees. It’s these little details that shield certain costs.

**What types of lease are available?** There are circumstances where a contractor might qualify for a leasing arrangement other than a finance lease or true lease. A good example of this would be, say, a tax-sheltered leasing arrangement which could have a substantial effect on interest payment costs.

**Who is the leasing company?** A contractor should find out the company’s ownership, financial strength, assets, experience in leasing the type of equipment you want.

**What are the leasing company’s documentation procedures?** Some companies must issue a separate lease for each new piece of equipment, while others provide a master lease with a series of amendments—or schedules—so a contractor may add subsequent pieces of equipment when wanted. This kind of documentation can have a noticeable impact on the amount of time and cost than a contractor will encounter should he want to arrange for additional equipment by leasing.

**With whom has the leasing company dealt?** On any leasing company being considered, a check should be made with other contractors or companies who have leased or dealt with the firm.

**How well financed is the leasing company?** Does the leasing company have sufficient funds for its operation or does it broker part of the lease to a third party? This is important during a money crunch because if the leasing company involves a third party and runs into trouble brokering its leasing paper, a contractor might have difficulty should he want to lease additional equipment.

In the final analysis, the efficient and profitable acquisition of capital equipment is the primary concern. Whether the contractor decides to buy from his own funds, borrow to buy, rent, or lease his goal is a profitable operation and the method of financing chosen must enable him to obtain equipment, keep pace with rising operating expenses and still function profitably.