A dollar here, there, it adds up

Yes, money is tight. But you may be overlooking one of your best sources for quick cash: Your business

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Editor

One of the facts of life in the operation of any business is that the bottom line is the final measure of life or death. But ask any contractor to vote for the financial item most critical to his business, and I’ll bet the answer is cash flow.

Even the most successful of businesses, no matter how rosy its profit picture may be, can see its growth or performance stymied by inadequate cash flow. The graveyard of commerce is littered with the corpses of great businesses which had huge amounts of fixed assets and product inventories at hand, but couldn’t come up with the day-to-day “small change” it takes to do business.

Cash flow problems in the construction industry are magnified today, because interest rates, tight money and the twin bugaboos of inflation and recession make every up-front dollar more valuable. Where lendable assets do exist in the short money supply, contractors are finding borrowing an expensive proposition. And, that interest expense goes straight to the operating ledger, and hence, right to the bottom line.

It is, of course, a reality of the construction business that fluctuations in the marketplace and the size of any major project’s capital requirements compel any contractor to borrow for interim financing. But, when a contractor finds himself borrowing small amounts of capital, even in short-term situations, in order to maintain cash flow, he’s increasing his direct costs of business, and he could be getting himself into real trouble.

There are a few basic management techniques a contractor can apply to his operation that can help to improve cash flow. These are small things, really, and individually, they won’t seem to amount to much. But, as the money is counted “a dollar here and a dollar there, it adds up.” You may not be able to finance your business operations on the savings these techniques can bring you, but you may be surprised by the overall results.

Too, even if you don’t use them to improve cash flow, you’ll realize increased dollar income, and you can take that straight to the bottom line, too.

Your bank accounts

It is certainly obvious there’s money in the bank. But if it is your money you’re talking about, it’s better you should be saving, not spending, your banked funds.

A lot of companies, for any number of good reasons, will maintain more than one account. That can result, however, in a restriction of cash flow.

If you use multiple accounts, check on service charges, cost of checks and banking forms, etc. Consolidating these accounts into one can result in direct savings.

Another problem with multiple accounts is that some will require minimum balances to be maintained. If these are consolidated into a single account, with a single minimum balance to be maintained, the result can be the freeing up of some capital.

If you maintain a large checking account to handle your payables, you can be costing yourself money. Move your payment dates to a particular day of each month, and in the meantime, don’t keep any more money in
Cash flow, when restricted, can deal a crippling blow . . .

your checking account than is absolutely necessary to the successful day-to-day operations of your business. Putting your funds into short-term, interest-bearing accounts will keep the money working for you until you need to move it into your bill-paying accounts.

And, if you occasionally use short-term loans for ready capital, get to know a loan officer at the bank where you do your other business. If you can gain a preferred customer status, it can save you through lower interest rates on short-term loans.

Your credit department

Accounts receivable dollars are almost as good as money in the bank. Generally, they are readily convertible to cash. You can use them as loan collateral or sell them outright through factoring.

But the real success story for your cash flow system lies in how effectively your credit department collects your receivables. The tighter control you maintain over credit and collection, the more cash you will have available.

If you offer a discount on invoices paid within a certain time frame (a 2% discount on 10 days is common), have your billing department verify that payment dates actually earn the discount. Some customers will take the discount, regardless of when the invoice is paid, and that can mean a cash loss to you.

When you are working out your contract, utilize phased payments whenever you can. If you’re dealing with a major job, it is likely you’re arranging incremental payment as the work is completed. With a little effort, you can do the same on smaller jobs, or in many cases, can arrange a partial payment of the contract before the work commences. That saves you money twice, because you don’t have to borrow capital at an interest expense.

Another place a good credit department can save you valuable cash is in evaluating the terms under which you allow your customer to pay. If you’re dealing with an “old, familiar” account, you may be accustomed to a particular payment schedule, so you won’t worry about being paid. However, if this payment schedule is causing you to carry your receivables balance forward for any extended period of time, you may be providing your account with a source of credit he couldn’t find anywhere else.

You may find that you’re earning some interest, which isn’t all bad, but you are effectively refinancing the
account’s obligation when you offer extended terms. If you’re looking for cash flow, you won’t find it here.

You can, by the way, turn a cash flow benefit from employing that same technique yourself. If you’re in a position where your own suppliers compete heavily for your purchasing power, you might find a salesman who is willing to allow you to pay on extended terms. This kind of arrangement is preferable to merely establishing trade credit, because trade credit buying can result in your paying unnecessary interest.

An example: If you purchase $5,000 worth of gypsum wallboard with a 2% discount if paid within 10 days of the invoice, you’ll save $100 with the prompt payment. However, if you take a full 30 days and pay the net, the extra 20 days cost you $100. If you were borrowing the $5,000 from a bank for the same 30 days, your interest expense (at 15%) would be only $62.50. In this case, trade credit buying costs you $37.50 more than conventional borrowing.

**Your operations**

Most contractors learned a long time ago that job control is a hedge against increasingly-expensive money. Changes in the methods of bidding, tighter estimating, better field management and acceleration of schedules became common to the industry.

Two key areas in which cash flow can be improved from the operational side are work progress reporting and job scheduling. A contractor can no longer afford even the smallest of mistakes in these two critical processes.

Knowing where a job is in progress pays the immediate benefit of avoiding costly overtime or work delays. It also, however, can have a drastic effect on cash flow by providing a well-phased schedule for the delivery and use of job materials, tools and segments of the labor force.

Job scheduling is obviously important to the contractor as a protection against overbooking of work. If the contractor knows when a job is supposed to be done and where it is in process, he has a winning system of comparatives. Job scheduling can also help the contractor’s cash flow in two additional ways. It can allow you to expand or contract labor forces in relation to production schedules. It can also keep you aware of any days you might gain in early completion of a phase, which could have a cumulative effect of bringing the job in earlier and speeding up the payoff.

The two processes also help inventory control, another big plus to cash flow. If you’re warehousing materials by the job, and some phase of work is being delayed—say for completion of the electrical installations—you might “loan” some of the materials (and labor) to another job to keep from losing the time and the cash investment in the materials.

If cash flow is a severe problem, inventory controls can also provide major relief through a temporary reduction in normal high-quantity stocks you don’t immediately need. And, if you’re overstocked on some items, you can convert some inventories to cash by selling them outright.

And, if you’ve been in business for any length of time, your operation probably has another ready source of quick cash: a storeroom. A quick inventory of unused office equipment, machinery, tools, etc. can bring extra money when you need it most. Any business that grows eventually outgrows some of its former equipment, and there’s usually a ready market among smaller, growing companies.

**Conclusion**

No business operator likes to think of himself in a position of needing cash so severely that it affects his ability to stay in business. But, like keeping adequate amounts of insurance coverage, it doesn’t hurt to be prepared.

The dependence of the construction industry on factors as complex as the economy or as simple as the changing of the seasons has developed a new breed of contractor. You are a skilled businessman. You’re an accomplished manager. As both, of course, you endeavor to always work within the capital available to you.

When the day arrives, however, that some market event or opportunity presents you with the need to expand your cash supply, you should have a complete grasp of where the money supply might be. It is certainly good business to explore the full range of outside funding, whether it be short or long term borrowing. But it doesn’t hurt, either, to examine the potential for better control of the cash within your own company.