Surviving Tough Times

Take these common-sense steps to help your business weather a slowdown

by Jim Cameron

My company had its most difficult year ever in 2007. The previous five years had been great: As a real estate developer and general contractor, I'd completed several successful development projects and worked with many repeat contracting customers. Business was so good, in fact, that I became less cautious than I should have been. I made mistakes — not saving enough cash, for example, and building a condo without doing sufficient market research on the location.

By late 2006 business had begun to slow down and I found myself struggling to pay taxes and meet loan payments. Those expenses had been manageable in a high revenue period, but now I found myself in a different world.

Since that point, I've put a great deal of effort into coming out the other side, and this effort has put my company on solid ground. And though there will surely be challenges ahead, I am confident I will survive and prosper.

This article outlines the lessons I learned during that struggle. It begins with the practices every business should have in place to prepare for tough times. I should have implemented them, I realize now, when times were good.

The article also describes the steps I took to recover. The challenges I faced are ones that could confront any small business; if you're already facing a slowdown, these steps could be the key to your survival.

Lean and Mean

A healthy business is resilient enough to respond quickly to market downturns and other threats. One of the major lessons I've learned over the last couple of years is that to stay resilient you have to run a company as if it were always in crisis: Keep expenses to a bare minimum and build up cash reserves and borrowing power.

Limiting expenses is the most important thing a company can do to prepare for challenges. That means limiting purchases and payroll to what's needed and not committing to monthly payments — for trucks, equipment,

or space — that can be sustained only when revenues are strong.

Ignoring this advice was one of my biggest mistakes. When business was good I invested in equipment I could easily have done without — new vehicles, for instance, and a new set of staging I hardly ever used and could have rented or borrowed.

A healthy cash reserve is a must; it will pay your bills when revenues fall.

I'm not saying that you should never buy a new truck — merely that you should do so only when your volume and margins are growing. To determine whether they are, you need to spend time realistically projecting future work volume and cash flow.

As for wages, I know a company that paid lead carpenters top dollar when they started working. This was helpful for recruiting experienced staff, but when revenues fell the company was committed to a high payroll. I pay my carpenters a lower starting salary than they can get elsewhere, but I compensate by offering regular raises, as well as bonuses based on the company's profitability. I am honest with my employees about our profits, so they understand the reasons for what they do and don't get.

Cash and Credit

Countless business articles recommend keeping six months' operating expenses on hand. This is like the advice to drink eight glasses of water every day: How many of us really do that? I certainly didn't. In the years leading up to my slowdown, I plowed most of my company earnings back into real estate investments. Big mistake! When my condo project didn't sell, my lack of cash reserves made it difficult to pay the mortgage on that property.

The fact is that a healthy cash reserve is a must if you want to be a survivor. When revenues fall, the reserve will pay your bills during the time it takes to adjust. At a minimum, you need enough cash to pay the basic expenses of staying in business: office rent, truck payments, workers' comp, liability insurance, phone, computer, and so forth. Exactly how many months' reserves you need is a figure you should discuss with your accountant and banker.

It takes discipline to put money aside to build up reserves, but it can be done. I had no cash at the beginning of 2007, but a year later I had managed to put three or four months' expenses in the bank. One way to make the process easier is to set up an automatic weekly or monthly money transfer from your business checking account to a CD or money market account.

Borrowing power is as important as cash, since most contractors fall back on credit when money is tight. The catch is that banks will typically lend only when you are in a strong or stable situation, with a track record in business, good cash flow, and some cash on hand (in other words, when you don't really need the money).

I suggest establishing a business line of credit (LOC) with your bank or credit union. A business LOC is similar to a home equity LOC in that it's secured by real estate, whether your home or an investment property you own. You can borrow from it at any time by writing a check. The minimum monthly payment is interest-only, though the banks I know usually require that you pay it down to a zero balance for a period of 30 days each year.

You should maximize the amount you can borrow and then be disciplined enough to use only what you need. If you are uncomfortable with this approach, establish the line of credit at a level you are comfortable with, and grow the amount over time.

When Things Get Tough

A lesson I learned years ago when I worked as a sales manager for another company is that you can rarely sell yourself out of a problem. Instead, you need to get your business into

shape and grow from there — which means identifying hard decisions and making them quickly. What follows are the actions I took to get my business back on its feet. No single one saved the day; success depended on a combination of all of them. If your business is in trouble, you need to decide which ones are right for your situation.

Everything is negotiable, even loans: Payments can be postponed and interest rates reviewed.

The necessary steps include those that require cooperation from business partners — suppliers, subcontractors, insurance companies, and banks — and those you can implement yourself. For many people, approaching a partner is difficult; they equate business struggles with failure and inadequacy. If you share this perception, you need to get over it — now. You are not the first contractor to struggle and you won't be the last, but if you start avoiding your business partners, your business is toast. The only way to survive and prosper is by taking action.

Suppliers and subs. Determine who needs to be paid and when. Then meet with all vendors and subs and present them with a plan for how much you can afford to pay against any old invoices, and how and when you will bring your accounts up-to-date. You don't need to reveal all the details of your business, but in some respects you are asking them to partner up with you.

I first saw this in action as a kid. My parents owned a retail store that extended credit to customers who sometimes were not able to pay as planned. My parents always said that as long as the customer paid something and communicated with them about the problem, they could work something out.

This still works today. For example, I have a contractor friend who was struggling to stay afloat four years ago, so he went to his supplier and worked out a payment plan. He is now back up and running and buying exclusively from that vendor. The supplier judged him to be creditworthy and realized that working with him was a wise investment.

It's very important that you commit to only what you know you can pay. If you can't make a commitment, be honest about when you can start paying. Without this kind of realism and honesty, you won't be able to emerge from a bad time with your financial reputation intact.

Review your insurance. Assuming that you have built a good relationship with your insurance agents, go meet with them. Review your deductibles and decide if any are too high or too low. Your agent can also contact the insurance carriers to discuss payment options, or can change your quarterly or semiannual payment to smaller monthly ones.

In some cases you may have to contact the carrier directly. I called one insurer to whom I owed several thousand dollars, told the representative what my situation was, and offered a payment plan. Her response was one of surprise: "No one calls us to resolve these problems." She promised to run it past her supervisor, who in less than five minutes called back to agree to my offer and to thank me for calling.

Renegotiate bank loans. Most people are reluctant to approach a bank, but in fact everything is negotiable, even loans. Monthly payments on mortgages and lines of credit can be postponed, and interest rates can be reviewed. However, you will need to have a good relationship with your bank and be willing to open your books to its officers.

The bank doesn't have to make any changes, but — like the supplier and insurer — it has an investment in your success. I suggest making your bank officer part of your business team by regularly meeting with him or her to look at your cash, cash flow, and debt ratios. This will

make the bank more willing to negotiate.

Sometimes you need to be persistent. I didn't have any luck renegotiating with my bank until I changed loan officers. It was worth the effort; my loan payments were reduced. And the bank is still making plenty of money from me.

Review labor and service costs. Take a hard look at the size and structure of your payroll. Do you really need a helper at each site? What services can you live without until things turn around? I unfortunately had to lay off two employees, and I cancelled all but one cellphone, as well as various other services.

Some of the best advisors are successful people who struggled in the past.

Sell assets. This was one of the most painful steps I had to take. I had spent six years buying and holding properties, and I saw those properties as tangible signs of my success. But in a crisis, the sale of a property — even one that is yielding positive cash flow — can bring in needed cash.

When I met with one of my advisors, we listed all of my properties on a dry-erase board, along with the cash flow I received from each. Based on that discussion, he advised that I sell three properties, including my home. After I got up off the floor, I put all three properties on the market. Three months after that meeting I had a sales contract on one property, and had rented my house (for twice the payment) and moved into one of my unsold condos.

Consider other types of work. This is common sense. When real estate stopped selling, I stepped back from property development into general contracting. I also stepped up a side business doing property inspections.

If you're a general contractor who used to do a lot of siding, you might have to go back to subbing out siding jobs from other contractors. My plumber has started taking work from a large developer who doesn't pay very well — which tells me the plumber's business is slowing down considerably.

You do what you have to do to survive.

Seeking Help

One last piece of advice: A fatal shortcoming among many small business owners is that they have few — if any — knowledgeable people to talk with about the nuts and bolts of their businesses. Don't be one of them. If you've read this far, you've noticed that I'm willing to talk with people about my business. That willingness was absolutely crucial to my ability to recover.

Make an effort to find people you can discuss business issues with on a regular basis, regardless of how well your company is doing. Some of the best advisors are successful people who struggled in the past. One of my friends had two companies fail before going on to start a very successful Internet business. Another friend went bankrupt in the mid-80s and is now running a successful construction company. I talk with both regularly about business issues and find those discussions invaluable.

Yet another friend referred me to a former bank president. I had only one conversation with this man, but he gave me some great information on what banks care about and how to deal with them.

If you don't know where to start, check with your local NAHB or NARI chapter, or call other builders you know. Ask your banker, your accountant, or the local small-business development center for referrals. Once you start asking, things will start to happen.

As an added incentive, remember that the process of bouncing ideas off other people helps you establish relationships and create opportunities you didn't have before. It's something you can't afford not to do.

Jim Cameron *is a real estate investor and general contractor based in East Fairfield, Vt.*