ANOTHER BRICK IN THE WALL!

The quantitative and qualitative considerations necessary to build your security guard business for current profitability and future value!

By H. Richard Dickinson, President, DICKINSON & Associates

Every time you successfully price a security guard contract, you have changed your company. These changes are often subtle; however, the decisions you make today will have a significant impact on the profitability and value of your company as you put more bricks in the wall!

As with all business owners, a day will come when you wish to retire and let someone else take those weekend calls. Whether you exit through a sale of your business, or pass it on to your family, you want the value at that point to be at a peak. In addition to equity and profitability, the value will be determined by several qualitative characteristics such as:

- Service Quality
- Client Profile
- Contract Tenure
- Contract Terms
- Client Concentration
- Client Retention
- Employee Retention

These characteristics are not built over night but rather over the life of your company. They are cumulative and can be either enhanced or diluted with each new contract you sell.

As a result, you need to build a growth plan that will steer your sales efforts in the right direction. Don't pick up your pen quite yet, however, because there are several key questions that should be answered before you begin:

Is your service better than your competition's?
If under bidding the competition is often the only way you can sell new business, you need to take a step backwards and realistically examine what your company has to offer.

Adding value in today's marketplace is essential. Hiring practices, drug screening, and initial as well as recurring training programs are all highly important to most sophisticated security users. Implementing solid programs such as these will not only enhance your sales efforts, but will help to reduce insurance rates and protect your company against litigation.

Client Evaluation, Quality Assurance, Officer Recognition and Employee Benefit programs are all examples of how a small company can add value to their service in order to pursue a more premium market segment and successfully compete with larger firms. What's more, these programs can be implemented quickly and at minimal cost.

What are your strengths?
Knowing your firm's strengths can save you valuable time and resources. Take a look at your current client list. If you find that a significant percentage of your hours are concentrated in one industry or market segment, you can leverage that experience and market your expertise in that area. This is especially true if there is a need for fast, short term growth. Diversifying your client list, while very important, is a longer term objective. Regardless, ALWAYS avoid high risk clients or industries.

Where should you grow?
Becoming a regional or national company is a common goal among many small company owners, however, expanding geographically is often tricky business. Multiple locations mean multiple sets of overhead costs. That new overhead must be covered by the gross profit from new contracts before any income falls to the bottom line. Saturating your current

markets first often makes more sense. As a rule of thumb, it takes 1,000 to 1,500 weekly hours to support a new stand-alone office. The gross profit from those same hours sold in your existing markets immediately produces pretax income while your new office has just reached the break even point.

A better way to enter a new market may be to find a self contained contract of 336 or 504 weekly hours, large enough to at least partially recover the cost of a site (or area) manager with sufficient ability to sell additional hours in close proximity.

How fast should you grow?
Unfortunately, it is often difficult to predict when opportunities will present themselves despite time spent on sales forecasts. Over the long term, however, it is important to control the growth of your company.

You should periodically assess the idle capacity of your operational and administrative staff, the excess space at your facility and the capacity of your billing, payroll and accounting systems. Each of these support functions will require additional investment at different points in the growth cycle and timing is all important. Plan your investments based on your forecasted growth and adjust that plan based on actual new business. A lack of timely investment in your support infrastructure can have disastrous effects over the long term.

Another option is to augment your internal growth with acquisitions. Finding one that makes sense strategically and that is reasonably priced is difficult, however it may also be a way of acquiring infrastructure that you currently lack.

How do you fund your growth?
When you begin a new contract, the funds you disburse for payroll, payroll taxes, uniforms, recruiting and screening expenses, and any required equipment represent a working capital investment. The amount of that investment grows until you receive the first payment from your new client. Assuming the client makes future payments consistent with your regular billing cycles, your working capital investment will not increase and, in fact, should decrease with each regular payment by an amount equal to the profit built into each invoice paid. The math is simple, the amount of each payment that exceeds the amount of payroll and other contract costs that must be disbursed until the next payment is received, is your cash profit which reduces the amount of the outstanding investment.

It is called an “investment” for a reason – those funds have to be available in order to begin that contract and they will be invested for a period of time. They have to come from the company’s existing cash or brought into the company from outside sources such as personal funds, bank borrowings, etc. Virtually every company has a finite amount of cash available for working capital investment so it is therefore essential that you consider all prospective business with caution.

Let’s take the example of a company currently operating at a break even with approximately $100,000 available for working capital investment. It is asked to submit two separate proposals, each for 1,500 weekly hours that would require similar direct and variable expenses including a $9.00 straight time pay rate. Using a typical cost structure, weekly costs would approximate $16,387 per week for each contract (before interest expense). Prospect #1 will only agree to 42 day payment terms. It is priced at a $14.50 per hour bill rate. The client offering contract #2 will agree to pay in 28 days but the company must price it at $13.50 per hour in order to be competitive. The first reaction by most business owners would be to go for the contract with the higher bill rate.

Proposal #	1	2	Extra
Weekly Hours	1,500	1,500	750
Bill Rate	$ 14.50	$ 13.50	$ 13.50
Weekly Profit	$5,363	$3,863	$1,931
Payment Terms (weeks)	6.0	4.0	4.0
Working Capital Required	$ 98,322	$ 65,548	$ 32,776
Recovery (weeks)	18	17	17

As indicated on the table above, contract #1 would use all of the available working capital. In addition, it would take 18 weeks to pay off their loan and begin accumulating cash profits of $5,363 per week. Naturally, for purposes of this exercise we have assumed that all costs and expenses are payable immediately.

If they instead chose to pursue Contract # 2, the weekly profits would be only $3,863 per week due to the lower bill rate. Please note however, that because of the more favorable payment terms, the working capital requirement is only $65,548. This would allow them to take on an extra 750 hours per week under the same terms without exceeding their working capital limit. Weekly cash profits would then climb to $5,794 ($3,863 + $1,931). Only 17 weeks would be required to pay off their bank loan and begin to accumulate cash profits.

The purpose of this illustration is simply to dramatize the impact of bill rates, profit margins, and payment terms on working capital requirements and therefore on your business. There are many dynamics to consider in pricing contracts as you grow your business. These will be discussed in a future publication of OnGuard.

H. Richard Dickinson is a Houston based management consultant focused on the security industry. His website is www.hrdickinson.com. He can be reached via email at Richard@hrdickiinson.com

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