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The Perfect Storm

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Can today's uncertain economic climate really have its opportunities?

While the manufacturing industry is finally beginning to show signs of a turnaround, uncertainty remains a chief concern. Economies around the world are grappling with debt crises, market volatility has become the norm and job growth can be measured by the decimal point. Meanwhile, financing is difficult to obtain, but not nearly as difficult as long-term contracts. Manufacturers across all sectors are fighting for long-term profitability amid a seemingly interminable cycle of fits and stops.

But what if this "perfect storm" of economic futility also had opportunities? What if the increased demand for lower pricing and higher production could usher in new efficiencies? What if the ever-tightening credit markets brought about newer, more innovative sources of capital?

When the perfect storm finally moves on, it will be the companies who used this time period as an opportunity to improve their operations that will grow and thrive.

Making Right Turns

In 2004, with fuel costs on the rise, UPS made an interesting discovery. The company realized that additional fuel was expended while drivers sat idle in left turn lanes. They contended that charting out routes with a preference for right turns would save on fuel consumption and, sometimes, even time.

Savvy manufacturers have managed to work smarter and faster by implementing a series of right turns into their own operations. This begins by eliminating wastes. Toyota recognizes "Seven Wastes" that compromise production: overproduction, waiting, transporting, inappropriate processing, unnecessary inventory, unnecessary motions and defects. Evaluating your company's production model against the Seven Wastes serves as a sound measuring tool by which to evaluate efficiency.

There are several key questions that should emerge from this process. First, what specific practices can be shored up to improve profit? Second, are there any customers or products that may actually be hindering overall profitability? And finally, what specific action items can be implemented to both reduce waste and improve overall profitability. Many companies may find that removing certain customers and products is the answer, while others will look to expand their services.

Of course, evaluation is only the first step in eliminating waste. The deployment of a waste reduction team provides the opportunity to implement a waste reduction plan, monitor ongoing operations and report milestones and progress to the company's owner or Board of Directors. The result of this process should be an efficient route through your business plan with more right turns to profitability.

Cash is Still King

When the economy began its downward spiral, it inadvertently shined a light on the importance of cash flow management. The thinning of profit margins, lack of available credit and overall reduction in contracts created a heightened sense of urgency for companies now struggling to remain cash flow positive.

While the crunch for cash continues to hang over virtually every manufacturer's balance sheet, there is also an opportunity to improve the management of cash flow and lay the foundation for higher profitability downstream.

This begins with the collections process and the management of receivables. Remain on top of outstanding receivables and create an iron-clad system to ensure the timely payment of invoices. For payables, adhere to a system of making payments near their due date, taking advantage of vendor discounts. Finally, pay close attention to order quantities to ensure you have the needed amount of product to complete the job but avoid running surpluses. Where possible, look toward implementing "just in time" inventory purchasing and handling processes to reduce the costs associated with storing and handling inventory.

The second part of the equation is credit. Traditional lines of credit are in high demand, but availability remains tight. This has led many manufacturers to look for alternative sources of capital. For companies in need of short-term cash flow, factoring agreements enable the sale of receivables to a finance company at a discount in return for immediate funding, eliminating the sometimes elongated wait times for customers' payments.

Purchase order financing has emerged as a viable financing option for companies in need of the cash to ramp up for a large contract. This enables for the procurement of financing based on an individual order to allow for the purchase of additional materials or labor necessary to complete the order.

Additional capital sources include letter of credit financing for international purchases and cash infusions from private equity sources. While all of these options hold higher interest rates and more aggressive terms than traditional bank financing, the volatility of the market and need to ramp up operations on a dime has stoked the demand for these more creative financing models.

The Great Differentiator

It is no mystery that in today's tight market, pricing reigns supreme. Customers are looking to partner with a manufacturer that can turn around the order quickly at the most competitive price. However, there are additional metrics that factor in to the decision-making equation that are easier to control, beginning with service.

One of the biggest oversights made by manufacturers in this challenging market has been placing their primary focus on efficiencies and cash flow, while losing sight of the customer relationship. This involves a dedication to meeting client needs on a day-to-day basis but also taking the time to strategically ask "what is my customer's biggest problem and how can I help them solve it?" The answer could represent a simple phone call, a small enhancement of your production process, the streamlining of your supply chain or even an entirely new service category that diversifies your offerings.

In an environment where every last unit can make or break profitability, downtime is often considered a dirty word. However, when used wisely, the decisions and adjustments made now can help secure a more productive and profitable future. With a redefined sense of purpose and a focus on improved efficiencies, now is the time to organically improve the health and vitality of your operations, your supply chain and ultimately, your bottom line.

Wayne R. Pinnell, CPA is the Managing Partner of Haskell & White, LLP, one of the largest independently owned accounting, auditing and tax consulting firms in Southern California, servicing public and private middle-market companies. Haskell & White works with companies in a broad range of industries including real estate, manufacturing, distribution, life science, technology, and retail. The firm provides solid expertise and services to its clients in the tax and audit disciplines, including advising SEC registrants and consulting on mergers and acquisitions.