Stu's View

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Major Equipment Purchasing, Part 2: Negotiation and Financing

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The economy may still be shaky, but have you considered that now might just be prime time for you to make that major equipment purchase you've been pondering? Yes, printing firms all around us have closed their doors under the financial pressure, and most printers have reduced staff and/or hours to contain costs. There's no denying it is a tough, competitive market out there; and yet the same market pressures that have driven us to cost cutting measures have also created a buyer's market in the major equipment arena. The decreased demand for major equipment has created some very attractive offerings in both the new and used equipment markets.

As noted in our preceding article, we are not advocating impulse buying here. Major equipment purchasing should always be done as part of your overall marketing plan, with full integration into the client base that you support and the products you can produce profitably. In our article, *Major Equipment Purchasing, Part 1: Before You Purchase*, we demonstrated that a purchase decision should be made only after a thorough financial analysis of its impact on your cash flow and your bottom line. Truly determine that you can afford to purchase. Even when bargains present themselves, remember to research, research, research the machines and maintenance/support programs available. Talk extensively to all reputable new and used equipment vendors and to current users of the equipment that you are considering. Understand the cost benefits, the capabilities, the warranties and consumable contracts, the training programs and environmental issues. Be sure you know and understand not only the tangible but the intangible concerns and costs.

Once you've done this important fact finding and financial analysis and know you can afford to enter the buyer's market, there are still two hurdles to face: Negotiations and Financing of your purchase.

Negotiations:

For optimum negotiation success, we recommend the following:

- Narrow your selections to no more than three final choices that meet your needs and goals.
- Establish a firm budget for expenses before you begin negotiations for the purchase and installation and base it on the numbers that have been discussed with each vendor -- then reduce that budget by 20% or some other percent to establish your target purchase price.
- Appraise any trade-in machine to determine the orderly liquidation value. This will give you some insight regarding any blind discount buried in the trade-in value offered by the vendor.
- Determine your payment options prior to negotiations. Have your lease or loan pre-approved prior to purchase to avoid embarrassing disappointment and the wasted time and effort of reaching an agreement, but then not being able to secure financing to pay for the unit.
- Explore vendor provided or supported finance or leasing programs prior to negotiations to determine terms and eligibility.
- Meet with each vendor, preferably someone at a senior manager or decision maker level, to discuss your budget limitations.
- Make the vendor aware that you are negotiating with his competitors.
- Establish a drop dead date for placing the order to motivate the vendor to get their best deal on the table quickly.
- Once you have the “best price” proposals from each vendor, go back for one more try, preferably within a few days of your drop dead date.

Financing Sources and Considerations

It’s well known that lenders are wary of financing printing equipment purchases in the current economic environment. Lenders have all suffered significant write-offs on printing industry loans, and collateral values for the assets securing loans have plummeted. Most printing firms have experienced significant reductions in revenue over the past 2-3 years as well, making regulated banks even less inclined to take them on as loan clients. There are still several financing sources worth exploring, however:

- Traditional bank loans may be more difficult to obtain, but if you have a good relationship with a commercial bank lender, discuss your needs and get a proposal. Be aware that banks will typically require significant additional collateral and personal guarantees unless you have a very strong balance sheet and present little risk of defaulting. If personal guarantees are required, be sure you go in with your eyes wide open. Lenders are no longer willing cut their losses when loans go into default, and there are some horror stories out there about printers who didn’t fully understand the consequences. Be very careful with personal guarantee requirements.

- Digital equipment purchases are often tied to consumable agreements and vendor service contracts, so the best financing arrangement may be leasing a unit through the vendor’s captive finance company. Many vendor finance programs include recourse agreements, repurchase agreements or other credit enhancements for the lender to assist the vendor. These programs allow the vendor to market to privately held companies that may have marginal credit.
- Although many of the traditional commercial finance companies that were lenders to the industry are no longer players, there are a few who are coming back in to the marketplace. Keep alert to changes. You should consult at least two commercial finance company lenders for proposals for the purpose of comparing all alternatives available to you. New Direction Partners and MargolisBecker can provide lender recommendations, if desired.

When considering financing packages, make sure to:

- Have a well-organized financial information package and purchase justification to present to any prospective lender before receiving a proposal. This expedites the process and saves time by resolving unrealistic expectations early in the process.
- Understand that the lowest cost financing may not always be the best choice. Collateral requirements, pre-payment or early termination penalties, lender-client relationships and deal structure are the most important considerations. Read before you sign!
- Understand the distinction between a secured loan and a lease:
    - A secured loan is akin to the mortgage on your house. In a secured loan the lender holds the collateral. They have a lien against it, and you amortize that loan down to zero through scheduled payments. You capitalize it on your balance sheet and it’s yours, subject to the lien.
    - A true lease, on the other hand, is a rental agreement where the lessor owns the equipment. Typically, they depreciate it and you do not capitalize it on your balance sheet. Through the payment of rent each month, the lender is covering their cost (really your cost) for depreciation and interest expense. The lessor’s tax benefit of ownership is factored into the payments, so while your apparent interest rate is very low, you have no benefits of ownership. We have found leases are beneficial when using high tech or IT equipment that you want to replace with updated technology three years down the road because of obsolescence.

In summary, consider taking advantage of today's attractive equipment pricing if it makes sense for you to do so. At all costs, avoid the "Buy it and they will come" mentality. Know your market and have your client base in place. Do financial assessment scenarios to see what you really can afford. Research the equipment options, negotiate purchase terms, and be very clear about financing obligations. Now may be an opportune time to consider a major equipment purchase – but as always, make your decision in light of what is best for your particular situation.

(*) "A Cup O' Joe is a complimentary teleconference series for printers offered by MargolisBecker on timely topics for the graphic communications industry. Details and registration forms for upcoming sessions are available at www.margolisbecker.com under the "Events" tab. Questions may be directed to Bonnie Pfaff at 888.577.1717 or bpfaff@margolisbecker.com

Stu's View is contributed by Stuart Margolis, CPA and Partner of MargolisBecker LLC to provide information that helps firms operate profitably. Major Equipment Purchasing: Part 1 and more information can be found at www.margolisbecker.com.

About MargolisBecker

MargolisBecker has long been recognized as the financial expert for the printing and allied graphic communications industry, assisting thousands of companies with strategic and financial management, valuation, mergers/acquisitions, accounting, audit and tax services. The firm is noted for its expertise in enabling printing companies to optimize profits. Proudly, it is the purveyor of the industry's *Cash is King*, and *Value-Added Principles of Management*, and compiles the annual Printing Industries of America Ratios, the industry's premier financial benchmarking tool.

About New Direction Partners

The team at New Direction Partners LLC has guided over 200 printing company owners through the sales and merger process. The advisory services reflect a full set of skills to help you sell or expand your business: valuation, management consulting, financial advisory and investment banking. The deep experience and industry expertise at New Direction makes it uniquely suited to serve printing, packaging and allied graphic arts businesses.