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The Education of an Evil Genius

Part 13

Money Management & Banking

One of my first tasks when I first came to the company was to figure out whether or not the CEO, who was in the top income tax bracket, should purchase a *low-yield but tax-free municipal bond* or a *bond with a higher yield but no tax exemption*.

This was one of my first encounters with "money management" at the firm.

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When the average consumer selects a bank, the deciding factors are generally things like *convenience*, *free checking* and the *free toaster* he gets for opening an account. If he's lucky, perhaps even a drop dead gorgeous teller.

The shrewd businessman also considers these factors: the financial condition of the bank, whether it is state-chartered or federal-chartered, its loan policy, other services, fees etc..

One of my later assignments was to analyze our "hidden" bank fees.

A bank cannot give "free checking" to a business. There are too many transactions! It costs the bank too much money to process everything. Therefore, the bank says something like this: *Okay, Mr. Businessman, we won't charge you for that, IF you maintain a minimum balance of such and such an amount.*

A close examination of a) the standard fees for these transactions, b) the number of your firm's transactions, and c) the minimum balance demanded by the bank to waive those fees reveals how much you are *really* paying for them in the form of "foregone interest".

Furthermore, any amount *over* the minimum balance becomes, in effect, *your interest free loan to the bank!*

When I finished the analysis and made my presentation to the CEO, I explained:

This "free loan to the bank" factor obviously reduces the effective yield on the minimum balance, because it is impossible for us to predict it precisely. The yield gets so low that it's actually cheaper to simply ignore it and accept the fees.

In our case, the savings weren't that big. We preferred to keep the safety margin inherent in the minimum balance. But at least we had explored the possibility and knew roughly what that safety margin was costing us.

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Our corporation's annual financial cycle resembled a wave.

Think of it like your utility bill:

In the winter, your heating gas bill (for the furnace) is high, but the electric bill is low.

In the spring, both are low.

In the summer, your gas bill is low, but your electric bill (for the air conditioner) is high.

In the autumn, both are low.

Part of the year, we had surplus cash, which we invested in Treasury Bills. Part of the year, we needed more working capital, which we would *gradually* borrow. *First* from the CEO at prime plus X%. *Then* from the bank at prime plus Y%.

Of course, there was a considerable difference between the interest rate on the Treasury Bills and the interest rate on the two sets of loans!

Monitoring the cash flow and keeping just enough funds available to meet short-term need - and parking the rest where it'll produce the highest yield – is the objective.

In consumer terms, think of it like this. Don't pay your bills *too long before the due date*. If you have too much surplus cash, pay off your credit cards instead of putting it in your savings account. (Naturally, pay off the ones with the *highest* interest rate *first*.)

This is what money management is all about. Even a small business can profit from this.

For example: Given a yield increase of, say, just 1%, this still comes to $10,000 per $1,000,000 in annual cash flow.

The CEO was already a very good businessman. He had a business degree. Nonetheless, *he had learned a lot about money management from my predecessor, the MBA!* Then he taught me. Money management became one of my *daily duties*. After doing this a few years, I fine-tuned our methods even more.

I adjusted the cost of money variable for the seasonal factor instead of using the constant of prime + X% throughout the whole year as had been taught me. The CEO spotted the change, asked me about it and then concurred with my reasoning.

Fantasy versus Lottery

Frankly, I would be absolutely ecstatic, if a small or medium size business CEO reading this would phone me.

I fantasize about the conversation going something like this:

CEO:
Hi, I liked your book! About that money management thing. We've never done much of that kind of thing. Can I hire you as a consultant? If so, what's your fee?

Me:
Thanks, I'm glad you liked my book. Yes, I would be very happy to do consultant work for you. My fee is 10% of the profit that results from either increasing revenue or reducing costs. YOU decide how much that is! …But I do request a copy of your calculations for my own information. After all, one or both of us might have missed something.

Imagine a company with $100,000,000 annual cash flow. If I can increase the effect yield by even *one hundredth of one percent* (0.0001%), the gain amounts to $10,000 per year. My own 10% cut would be $1,000…If I can boost this to one whole percent (1%), that's a $1,000,000 gain and my cut would be $100,000.

CEO:
What's the catch?

ME:
No catch! I read about another consultant, in another industry, who routinely made the same offer. He did very well. His clients were also very happy. I'm will-

ing do the same thing!

No joke! I'm dead serious!

Some people play the lottery. This is simply my alternative.

Of course, the huge Fortune 500 Companies have a *Chief Financial Officer* (CFO) who does all this much better than I ever could. After all, he's a *specialist* in this field. Whereas I am a *generalist.*

Bank Selection

One day the CEO summoned the General Manager and me. He showed us an article about our current bank. It pointed out troublesome indications that something wasn't right.

I'm worried. I've noticed two more bad signs. First, every time our loan officer comes out to visit us, it's a different person. And their loan offers are too good. Something is wrong there. I think it's time we start looking for a new bank.

A tip on bank selection: Look at the "recovered debt". If it is conspicuously low, this is a warning sign. A healthy bank is sooner inclined to write off a debt as bad – and hence recovers a larger portion of debt already written off – than an ailing bank.

We proceeded as follows:

First, researched for tips on bank selection.

Second, looked at the *financial statements* of several banks in the area.

Third, met with the bankers.

In the end, we opened accounts at *three* banks: one for day-to-day banking, one for larger transactions and one for letters of credit for our import/export operation.

There can be a HUGE difference between banks. (I remembered this the next time I purchased a house.)

By the way, the same thing is true for printing companies. We used *three different printing companies* for the *same flier* depending on the quantity needed.

Inheritance

After I'd been at the firm for several years, I made the following suggestion to the CEO:

One day your children will inherit the company. You've already told us that they have no interest in running it themselves. If they hire somebody else to run it for them, they run the risk of losing everything. So they'll probably want to sell it.

However, there is a problem. The prospective buyers will probably be interested in only one or the other of the divisions. Not the whole package. But our company is so complicated and intertwined that this would not be possible. And if the firm is cannibalized, the value is much less than if it is sold as an ongoing, profitable concern.

This package deal, however, would be much more attractive to a prospective buyer, if the firm had an established line of credit WITHOUT you having to personally co-sign the bank loans.

He thought about this and agreed.

So we started the search for the *right* bank for this.

Then a Vice President from one of the big banks visited us. The CEO, General Manager and I were at that meeting.

Finally, only *one obstacle* remained:

The bank's "boiler plate" contract gave it the right to call in the loan - at any time, for any reason and at its sole discretion (!) – with only a *24 hour* notice.

My CEO insisted on a *48 hour* notice. He said he would need the extra day to make arrangements.

The banker promised to check their legal department and call back.

When the phone rang, the banker told us two things:

First, the bank's lawyers would *not* change the standard contract.

Second, we had done a better job preparing for the negotiation than many firms *ten times our size!*

It was not the end of the world. We didn't need that credit line to carry on.

But I was a disappointed. I had envisioned the senior executives one day joining together to buy the company. The other two had worked there for their whole adult life. They would *never* land a comparable position elsewhere. One of them said this to me outright. The other one certainly also knew it. We were all confident that the three of us together could indeed run it. Because we were *already* running it by then.

Give Credit Where Credit is Due

Back then, the credit reports that crossed my desk showed a detailed credit history. Not just a “score”.

When I was a trainee, the CEO would decline credit, if he saw a single default listed on a report. Later I convinced him to modify this policy: If there were numerous satisfactory listings and only one default – and it was on a *big medical bill* – I would recommend credit approval.

The CEO also taught us to consider “industry standards”. They vary.

Furthermore, if bad debt is *too low*, it may indicate credit policy is *too strict*, which can result in lost sales!

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Not long before the Great Recession, I was planning to buy a house, so I checked out my mortgage options. I knew I had an excellent payment history and large unsecured personal lines of credit. But I also had a lot of debt and my personal income wasn’t as high as it had once been.

Nonetheless, when one bank offered me *twice* the amount I needed with *zero down paymen*t, I was stunned.

One banker told me: *Yes, you qualify. Your credit is great! You have two options: For Option A, you have to supply copies of your tax returns to prove your income. For Option B, you simply TELL us your income. You don’t have to PROVE it. You can tell us any amount you want to qualify for any mortgage you want. Naturally, the interest rate is higher for Option B.*

I couldn’t believe this insanity! No wonder the nation’s economy went down the toilet!

The CEO’s Strange Dilemma

One day the CEO summoned all the senior staff. He had a grim expression on his face. None of us knew what this was all about. He portrayed his dilemma pretty much as follows:

Look, it’s like this. My wife is nagging me to hire our son as a consultant. He’s trying to establish his own consulting practice and needs the money. I don’t want to hire him. But I want to get my wife off my back, so I’ve agreed to it. Just play along. Don’t say anything.

I was reminded of the interview with the fresh college grad who didn’t want to share his infinite wisdom with us free of charge. But this was worse! The father had put his son through Harvard Business School. He now had an MBA. He was destined to inherit a large share in the business some day. Instead of learning about his family's business even *in his own best interest*, he expected his father to *pay* him for it in the form of a hefty consultant fee!

I could tell the other executives were thinking the same thing. One even told me so after the meeting, using almost the same exact phrasing as I have here. All of us felt sorry for the CEO and promised to play ball.

While the son "consulted" at the company during the next few days, we tried to give him at least a very basic idea of the business.

Then the CEO scheduled a big staff meeting. He had told me the previous day to prepare a presentation and to keep it simple. The son was the only one there who didn't realize all this was just a big show for his benefit. Everything I expounded was common knowledge for the rest of us. Kind of like a conference for astronomers, where the keynote speaker slowly explains: "The sun is at the center of our solar system. The planet closest to the sun is Mercury. The second planet is Venus…".

I made an extra effort to speak slowly and keep everything as simple as possible. After explaining a simple equation, he politely interrupted me with a slight, but still perceivable, air of superiority:

"Excuse me, but you said TWO TENTHS of one percent. Surely you actually mean TWO percent. Two per HUNDRED, not two per THOUSAND."

We all had to bite our tongue to keep from laughing. The CEO struggled to conceal his own embarrassment at his clueless son's blunder. (He was off by a magnitude of ten.) The CEO muttered something and motioned for me to continue.

This reminded me of the time that I had humiliated the IBM expert. Except in reverse. And even worse: At least the IBM expert realized he had made a mistake and had been caught. The son, an MBA (!), did not.

Reputation & Clout

Reputation is something you *build* through *past* achievements. *Clout* is something you *use* for *future* achievements. In my case, they had three main sources:

First, demographic analyses resulting in substantially reduced selling expenses.

Second, new product development resulting in huge sale boosts. Examples are both my first top selling product, which I discovered early on while attending a trade show on my own time, and my very last product, which was launched just after my departure.

Third, problem solving through analysis.

Here are a few illuminating examples.

Incident One: Persuasion

It was a grueling meeting for the four of us senior executives. The problem was complicated. The discussion wasn't making much progress.

Then I presented my analysis of the situation. Slowly. After each step, I checked each face for comprehension and agreement.

The CEO commented: *He cut through the bullshit and got down to the bottom of it!*

Next, I attempted to explain my proposed solution. But it was hard to grasp.

Then I remembered a much earlier meeting, where the CEO had dramatically grabbed a piece a paper, spit on it, crumbled it up and scorned: *It ain't worth spit!*

I reached into my pocket, pulled out some loose change and slammed the coins onto the CEO's desk. Then I used those coins to illustrate my explanation.

Soon the CEO agreed with my proposed solution.

A little while later, he came to my desk, looked me in the eye and said: *You convinced me, when you showed me with those coins!*

Incident Two: *Boy, are you going to get it!*

The CEO was not in the plant that day. An unusual situation came up. It wasn't a perfect match for any existing Standard Operating Procedure (SOP). So the General Manager asked me, but wasn't completely at ease with my answer.

I'm not a mind reader, but I could read this face: *Okay, I'll do that. When the CEO gets back, I'll tell him YOU told me to do this. BOY, ARE GOING TO GET IT!*

When the CEO returned, the General Manager explained everything. The CEO reflected a moment and then said: *You did the right thing!*

The General Manager was surprised. I wasn't. I knew why I was right. And I knew the CEO was smart enough to understand the reasons behind SOP, not just memorize it and blindly follow it.

Incident Three: Top Dog

Not long after this, all four senior executives were in a meeting. The CEO instructed the other two: *If anything ever comes up when I'm not here and you don't know what to do, ask HIM and do what he says!* He was pointing at *me.*

Incident Four: A Big Compliment

You have an Yiddish mind!

The CEO was obviously very impressed by my achievement. This was a BIG compliment. I knew this very well. It was completely sincere, much appreciated and highly ironic.

My Departure

I finally left the company after roughly a decade – on my own initiative and on good terms, NOT fired! It was still roughly about the same size in terms of gross annual sales. Divisions and markets had ebbed and waned, but balanced each other out overall. Top selling products had become has-beens and upstart products had become super stars.

When I phoned months later and asked how things were going, the General Manager said: *"Great, thanks to you!"*

At first, I didn't know what to make of that. Were things going great, *because I was gone*?!?

But no…

The last product I had conceived and championed before leaving – it had been launched shortly after I left - had produced a *quarter of a million dollars in sales within those few months*.

I was happy to have given the company a kind of "reverse going away present".

If I had stayed on one more year, another five-digit bonus would have been pretty certain. But I still didn't regret returning home.

However, the Iron Curtain had fallen. Duty called!

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