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Increasing Company ROI through Smarter Purchasing

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Although it's been four years since Hurricane Katrina tore through the Gulf Coast, people in and around New Orleans are still restoring what they lost. Helping them rebuild is Hammurabi, a Miami-based collaborative of designers, architects, engineers, consultants and construction professionals that opened an office in New Orleans after the storm. Since then, the company has been building hurricane-resistant structures throughout south Louisiana, where geography has created a slew of unique challenges.

Among the most significant has been procurement, according to Alan Macken, Hammurabi's principal. "We're building in an area where materials and people are scarce," he says. "Because we can't count on the infrastructure that we're used to, it's really important that we think carefully about the supplies we need. If you lose a saw blade and you're an hour and a half away from the closest place to buy one, that's a lot of lost time and productivity."

In post-Katrina Louisiana, planning purchases is especially important. Even in the most populated communities, however, builders must pay close attention to the money they spend on materials and supplies, says Macken. "You've got to control your materials costs, and when you take the time to properly plan out your job it's easy to see how."

Cash flow is king

Materials costs are so important because they're so large, according to small business consultant Terry Justice, president of Keystone Financial Consulting. "Aside from payroll, your supply costs are generally your next largest expenditure," he says. "For small businesses, cash is king. You've got to make sure you're monitoring and managing your cash flow appropriately."

When business owners spend money on supplies, they're converting it into inventory,

Justice explains—and you can't use inventory to make payroll or pay bills. To cover the costs of doing business, they need cash.

“Smart procurement means either you're negotiating stronger contracts so that you're buying at cheaper prices, or you're finding great deals so that you're able to purchase at a discounted price,” Justice says. “Either way, you're reducing your overall cash-out-of-pocket expense so you can increase your profits.”

Spend less, make more

According to Macken, increasing return on materials investment requires knowing exactly what you need, how much you need and when you need it. “You need to understand what your demands are,” he says. “For every job you do, you've got to know on a daily basis what you need and what you've got.”

In addition to knowing what to buy, you've got to know how to buy, according to professional negotiator Jeff Gordon. In order to spend less and make more, he offers the following procurement tips:

- **Buy in bulk:** While buying in bulk almost always results in a lowered per-item price, it requires careful planning, says Gordon. “It's only cost-effective if you're going to be able to use what you've purchased in a timely manner,” he says.
- **Buy in advance:** Although doing so may allow you to take advantage of bulk or pre-payment discounts, pre-buying materials isn't always a good idea, Gordon says, because it typically means buying supplies you don't currently need and spending money to store them, particularly on job sites where theft can be a problem. “If you have to spend more money than you currently have, or more money to store the unused materials, then that's going to decrease your ROI,” he says.
- **Consider automatic purchasing systems:** Automatic purchasing systems, which automatically replenish dwindling inventory, are a double-edged sword, according to Gordon. “For large organizations, the cost savings you realize is in the automation,” he says. “For a small business, any type of system of this nature is going to require at least one person to run it—and that same person could've been spending their time actually buying the materials rather than running the system.”

Buying power

Because some of the most popular procurement techniques—pre-buying and buying in bulk—can also be the most risky, Macken, Justice and Gordon suggest falling back on the following, more traditional purchasing techniques in order to maximize buying power:

- **Know your vendors:** Macken recommends investing not only in supplies, but also in relationships with the people you buy them from, as vendors are more likely to give discounts and flexible payment terms to customers they know and like.
- **Act bigger than you are:** Like their largest competitors, small businesses can submit RFPs to multiple vendors, according to Gordon, who says more competition often leads to better pricing.
- **Buddy up:** Although their size makes bulk purchasing difficult, small businesses can tap into bulk buying opportunities with fewer risks, Justice says, by joining a buying consortium, which consists of many small businesses that join forces in order to negotiate bulk discounts on materials they all can use.

Although low prices are great, having a strategy is more important than finding a sale.

“When you take a look at your balance sheet, there’s three things you’re paying attention to,” Gordon says. “The amount of money coming in, the amount of money going out and therefore the amount of money you get to keep at the end of the day. Every dollar you spend is one dollar fewer you get to put in your pocket.”