

# In The Trenches\_ Interview with Nicholas Andrews

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## SUMMARY KEYWORDS

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## SPEAKERS

Steve Divitkos, Nicholas Andrews

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**S** Steve Divitkos 00:00  
Nick Andrews, welcome to the show.

**N** Nicholas Andrews 00:03  
Thank you for having me, Steve.

**S** Steve Divitkos 00:03  
So we've got a lot to talk about today, I should say. And the reason why I wanted to produce this particular show is in light of what is happening from a macro economic standpoint, CEOs and CFOs have a lot of considerations that I'm sure are weighing heavily on them. And where I wanted to start, Nick, in light of what's happening from a macroeconomic standpoint, is everything to do with cash and liquidity management. So I want to start out with what might be a very basic question. And that question is, how should CEOs think about how much cash to keep on their balance sheet at any given time. And I remember, you know, when I was a CEO, there was a bit of push and pull on one hand, a lot of cash always provide me with a lot of buffer or cushion against unexpected negative events. But on the other hand, maybe at the opposite end of the spectrum, too much cash on hand can be seen as overly conservative, perhaps not an efficient use of capital? So where do you stand on this? How should CEOs think about this question?

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Nicholas Andrews 01:14

Yeah, I think it's going to, you know, vary based on the type of business that you're running. But, you know, my starting point, for any type of analysis around how much cash to keep on the balance sheet, would. I'd look back at, you know, kind of my historical performance, look back over a year, whatever time period, you know, you want to pick. And look at the nature of my business, because, you know, some months are going to be, you know, common have cash rich months, and some months are going to be cash lean months. So if I start with a framework of knowing that I've got maybe six months out of the year, that are cash rich months, and six months out of there, that are my cash lean months, you know, I might use that as a starting point to say, I probably need to build up a buffer of six months of reserves. But I wouldn't just do that alone, I would look at my historical nature of the business. And then I would also look at how my business is performing. And so for me, you know, one of the things that I'm always focused on, and some of the metrics that I'm always kind of running in the background are around working capital management. So I look at the cash conversion cycle pretty quickly, or pretty frequently to see how quickly are we collecting money? So if I go back to what what I said earlier, if we have six rich months and six lean months, and I say, Oh, well, I, you know, I need six months of reserves. But if I run the cash conversion formula, and I say, Oh, well, my conversion has actually gone down. So I actually need to have maybe seven months of reserves, or eight months of reserves. So I would use historical nature. And then I would look at how the business is performing to determine maybe how much cash I would need to keep on the balance sheet. Once I have those two foundational components, I would look then at kind of what my burn rate is, how this year is changing for maybe last year, look at my burn rate, and then look at how my cost structure is either changing or evolving over prior years. And use that information to come up with what a comfortable position would be for me to hold cash on the balance sheet.

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Steve Divitkos 03:18

And you mentioned the concept of months of reserves. within that framework, what are we measuring? So as to another way, are we talking about a certain number of months worth of fixed costs to have in the cash in the bank in the form of cash or a certain number of months worth of payroll? Maybe some CEOs would say a certain percentage of sales? Like are there any metrics or rules of thumb that you would look at elsewhere in the financial statements that inform or guide the dollar value of cash that you want sitting on your balance sheet at any given time?

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Nicholas Andrews 03:56

Yeah, and it's very interesting, because I actually just had a conversation with a CEO about this. They're in a service based business. And, you know, one of the things we were just talking through was, you know, they've got the cost to run their business. So they get hired to do a job, they have the direct cost for them to produce that job. And then that profit is what has to cover the rest of their, you know, overhead expenses. And they didn't know what that burn rate was. So I calculated that burn rate for them. And I just said, Hey, this is what you got to have in per month. And given that number, the CEO said me, I've never thought about it in that way. And so from that standpoint, for them, it was it was direct overhead costs of what their burn rate was, and then they could look at that and say, Okay, well, I'm comfortable now having three months of my overhead costs. I think you can look at, you can use metrics, but I think you have to look at metrics holistically. So one of the things you mentioned was percent of sales. You could look at percent of sales and having that in reserve, but I would also look at percent of sales in terms of my collections too. So if I'm looking got sales plus my collection rate. So if I have a certain number of sales, and it's taking me 30 or 45 days to collect those sales, I would want to look at those two items in tandem in order to calculate what my reserve would be. Because if I just said, it's three months of sales that I want to keep, but it's taking me 90 days to collect sales, I need to make sure that I have the buffer to manage those sales, knowing that it's not going to be coming in for 90 days. So I usually look at metrics in tandem. So I usually look at things and how they affect the income statement, as well as the balance sheet when I'm looking at kind of my rule of thumb.

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Steve Divitkos 05:37

Now, you know, excess cash sitting on the balance sheet, I guess in theory and in practice, loses value to inflation, in theory every day. So, does the current inflationary environment as of this recording? I think it's in the neighborhood of nine or 10%, which is as high as I've ever seen it. Does the current inflationary environment color your view of this in any way, so said another way, you know, going into macroeconomic uncertainty, perhaps going into a recession, that would suggest that CEOs would probably be wise to keep a lot of cash on their balance sheet. However, high inflationary environment would suggest pretty much the opposite. Because that cash is just losing value daily to inflation. So it seems like CEOs and CFOs are kind of getting conflicting messages from a macroeconomic standpoint, how do you kind of reconcile those in your head? And does the current inflationary environment impact your answer in any way?

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Nicholas Andrews 06:49

Yeah, I mean, you hit on it. Yeah. I think CPI data, you know, on Wednesday was like, 9.1%, if you think back of the forecasts, I mean, I think they forecasted flat CPI. You know, and I think the month over month change in headline inflation was one point something percent. So yeah, I mean, that weighs on my mind. And it's inflation that we haven't seen in 40 years. So I think it's a delicate balancing act, when thinking about how much cash keep on the balance sheet. And if you've got excess cash on the balance sheet, and, you know, you're looking for ways to maybe protect yourself in an inflationary environment, what I would try and do is I would try and look at how the business is running, and maybe really kind of challenge the status quo to say, are there ways that I could maybe protect myself from this cash? Because trying to get a return on that cash, both with interest rates, where they're at is difficult. So it's tough to say, well, I've got excess cash, I can park it in, short duration, vehicles to earn, some nominal, you know, rate of return, but on a on a real basis, you're still, you know, negative. So, if I was like a manufacturing company, you know, I'd be looking at my business saying, you know, are there any ways where I could maybe protect myself from further inflationary pressures? Could I lock in purchase contracts? Or can I lock in prices for items that I'm going to be buying in the future? If I look out over the business, and I know I'm going to be having cash outflows Is there any way I can protect myself now from further increases inflation is probably how I would be approaching it. Just given the fact that, you know, trying to find a return or trying to find a way to offset the destruction of inflation is going to be very difficult right now. I'd also be looking at how this will probably impact my customer base, because, you know, we're, I mean, I've, my view is that we are headed for a recession. Now, I don't know when that's going to hit. But I probably look at my customer base, and trying to assess just how strong my customers are, and see how you know that, that recession might affect them. So that way, I can maybe model out and forecast how it might affect my business. That's how I would look at it.

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Steve Divitkos 09:03

Now there are more components to liquidity than just the dollar value of cash sitting in one bank account. And CEOs have a lot of levers at their disposal to potentially increase liquidity to the extent that that's something that that they want to do. You know, in our last episode, I spoke with Jim Sharp about raising prices, of course, you can raise volumes, you can decrease your cost, you can stretch your payables, you can accelerate your receivables. I mean, you know, these are kind of pretty common levers, but but they're not all necessarily created equally. So, in your experience managing liquidity crunches, or at least in anticipation of liquidity crunches, what are some of the levers that you've pulled that you found to be particularly impactful that CEOs might want to consider doing right now?

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Nicholas Andrews 09:54

Yeah, I think it's really kind of interesting if you know have the ability to raise price and not face demand destruction, I think that that's a, you know, a good way to go, it can be kind of a delicate balance is if you raise price and you face demand destruction reversing that course, you could permanently lose business. The volumes, when I think about raising volumes, my focus there would be really focused on, you know, breakeven analysis. I was actually just working with one of my clients on this looking at breakeven for them across some of their product lines. And in order for them to achieve breakeven, they would have had to scale up their production to add a whole other line of manufacturing. And so when you add a whole other line of manufacturing, that's obviously going to change because you're adding additional fixed costs. So, raising volumes is always, it's a way you can, you know, increase cash coming in. But I think understanding how that's going to change your breakeven point, and your overall cost structure is very important. For me, my kind of first places, I always look inwardly, within the business. So one of the analysis that, you know, I would say to do is, if you looked at, say, increasing price, or just increasing volumes, I would compare that to how quickly we're collecting on our sales. I mentioned earlier, if you have a long collection time, you know, increasing price, you would probably face some demand destruction, but you would have, you know, eventually more sales coming in. But if you're collecting your sales on, say, 90 days, what happens if you collect your sales on 85 days? And you have to look at the change, and like, what would what would potentially generate more cash for the business, sometimes just changing your collection, your collection on the business, or managing your working capital more efficiently, will actually be create more cash for the business than, say, changing prices or changing volume. So I kind of start there as my baseline of looking at the efficiency of AR, AP and inventory management, and then saying, well, what happens if we just change some of those? So we keep our prices, we keep all our customers the same? But what happens if we just speed up collection by, you know, one day, two days, three days, what does that do for us in terms of cash in the business? Sometimes that can be more impactful without putting a shock through your customers of, hey, here's a price increase, or trying to go create more demand within the market, if demand saturated in the market for your product, raising volumes might not necessarily be an option.

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Steve Divitkos 12:29

What about like the 2/10, net 20 structure, which would say that, hey, we'll give you a 2% discount, if you pay within 10 days, otherwise pay us within 30 days at full price? You know, that has always kind of struck me as for lack of a better way to put it a bit of a desperate move. And what I mean by that is, it strikes me that a CEO would have to be in a pretty desperate liquidity situation, to do something like that. Am I incorrect in that assumption? I mean, how have you used early payment discounts, if at all, while historically managing a liquidity crunch?

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Nicholas Andrews 13:08

So I've never had to use them to manage liquidity crunch. I've always been on the other side. So I would answer it from kind of the other side, any scenario where we've offered a 210, like you just mentioned, you take advantage of it, because when you annualize that return, it is significant. The savings that you're that you're getting, I mean, sometimes, you know, when people hear it, they go, well, it's not that much. But you have to realize that that's over a 10 day period, and you have to put that into terms of the year. And that's a significant discount. So if I was, if I'm on the other side of it, I'm real hesitant to be offering discounts on payment terms, you know, if there's ways to speed up collection. I think there's other levers that you can pull, maybe it's volume service, other ways that you can maybe help drive a collection rate, without offering a discount. To me, unless it's maybe industry standard, or something very, very specific, you know, I would shy away from offering discounts unless it's absolutely necessary. So, kind of like you mentioned at the beginning of the question, it's something that I think would be a last resort of what I would advise someone to do.

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Steve Divitkos 14:22

And you talked a lot about the volume lever. And in speaking to CEOs in the past, when the question of increasing volumes comes up, the response tends to be something to the effect of, oh, you know, you want me to raise volumes. Well, what a profound insight like what CEO is not trying to raise volumes, but as I think about pulling the volume lever, tell me if I'm thinking about this, correct. I mean, there's a couple of things that I would consider as a CEO to figure out whether or not this is a lever I should be pulling. So first is my collections, right? When I provide my product or service do I collect all up front or do I collect let's say, after the service is provided or after the product is provided? Two would be the margin, the gross margin, do I have a high gross margin that I can eat into? Or do I have a low gross margin that I really can't eat into otherwise the sale would be unprofitable? And last is like the payback period of a customer acquisition costs. So for if it cost me \$100, to acquire a customer, but I can get that \$100 back in two or three months, that's a totally different story than if it takes me a year to get that. So I guess, you know, part one of the question, Am I thinking about that right? And two, are there any other variables that CEOs should consider specific to increasing that volume lever?

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Nicholas Andrews 15:43

Yeah, you know, I think the items you mentioned, are those would all be the same items that I would look at as well. I mean, if if you could just raise demand, that, to me implies that there's, you know, you're taking market share at that point. So, is your is the demand for your products such that it could go from, you know, 100 units to 120 units? And are you taking those extra additional 20 units that you're putting into the market? Are you taking those from a competitor are those truly unfilled, you know, demand in the market. I think the only item I would maybe add to the analysis around increasing demand, or increasing volumes would be the purchasing decision. So how much inventory now you're going to be needing to buy and what that's going to do to your purchasing? So, if I have a lead time, you know, going back to my example, if I was doing 100 units, if I have a certain lead time and a certain price structure that I've worked out with my supplier, how does that lead time and price structure change? If I need to now be buying more units? And then what is that going to be doing to going back to what I said earlier about my cash conversion cycle? So my inventory on hand, so looking at how quickly I can, you know, sell those additional units into the market and what that does to my overall collection? I think that's the additional analysis, I would do around that and figure out if I have the working capital to support that, am I going to need? Do I have to take on maybe bank debt to buy the additional units of material? Or how can I find that internally?

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Steve Divitkos 17:13

Let's talk about the opposite side of the coin. We've been talking about levers to pull to increase liquidity. But there are variables that can decrease liquidity, some are more obvious than others. And I remember speaking to a former investor of mine who called these cash vampires, which is to say, these are less obvious drains or uses of cash that maybe aren't always on the radar of CEOs. When I kind of, say cash vampire, or a less obvious use or drain of cash, does anything come to mind in your experience?

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Nicholas Andrews 17:51

Yeah, I think there's a few, I would say some of the cash vampires like one of them is, can be PTO, can be a cash vampire. I was speaking with someone the other day, and they were a manufacturing company, they mentioned, you know, the holiday just happened. And then they had some of their production, like, I think the majority of their production staff was out the whole week off as well. So if you think about that, you know, you're still incurring cash outflows because you're having to incur that the wage costs for that, they're not their productivity would, you know, maybe decrease, or maybe you've got the ability to sustain that. But if you don't have the people that are producing the product, you know, then you're gonna have a drop there. So, PTO is one of them. And if you have a significant sized company, I mean, that that liability can be hundreds of 1000s to, you know, potentially up to millions of dollars per year. The other the other cash vampires that kind of fall off the radar, you know, or corporate credit cards, or lax expense policies, that can be a big one. Because maybe you have, you know, spending thresholds, like you have to get spending approval above a certain threshold, but if I've got a corporate credit card and I'm a part of a team that's out meeting with clients and I'm kind of doing lunches here and there and stuff that's under the radar, all the sudden I could have cash go out the door that can be more than anticipated. And then you're not knowing about it until you know, maybe they're when an expense report is filed, or maybe to when you see their credit card statement. So those are things that can kind of catch you. Other cash vampires that I've seen have just been like a decentralization in spending. So you know, someone's responsible for maybe ordering supplies for the business but they just say like, oh, well, this so and so needed a chair so I bought a chair so and so I needed a computer. So I bought a computer. So when you have these kind of decentralized policies or maybe decision making, that can be a cash vampire. And then the other one that I kind of see sometimes, as you know, in this is I'll need to expand on this. But sometimes if you're managing your ratios, your ratios can kind of act as cash vampires, and one that can kind of act as a cash vampires your current ratio, because it can be a little misleading when you think about your current ratio. If you have a big numerator and that scenario, but if that numerator is being driven by inventory and AR, you can have a strong current ratio compared to maybe you're benchmarking against your competitors. But if you're having you know, those two areas, you know, that are significantly higher in a lower AP that can act as a cash vampire until you can get those items collected, or that inventory sold.

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Steve Divitkos 20:42

A current ratio defined as current assets divided by current liabilities, right?

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Nicholas Andrews 20:46

Yeah, exactly.

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Steve Divitkos 20:47

And so it sounds like what you're saying, which is intuitive is that growth in the current ratio to the extent that one is managing towards it, they're not all growth is created equally, if the growth is coming from uncollected receivables, or a bunch of inventory that you've bought, that's growth in the current ratio is not necessarily a good thing.

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Nicholas Andrews 21:04

Correct. Yeah. Correct. You have to look at the components of that. And now if it's all cash, and you know, no ar and no inventory, then yeah, that's not a cash vampire. But if you look at it, and if you're looking at your current ratio over time, and it's strengthening, and if it's strengthening due to AR and inventory, then that's a cash vampire in the business.

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Steve Divitkos 21:22

So I wouldn't be surprised if CEOs around the world are paying a lot more attention to cash and liquidity today than they were, you know, let's say six months ago, with good reason, as we've discussed. But to get really tactical. What should CEOs do, to the extent that there are tactical practices or exercises that let's say every small business CEO should actually engage in that would maybe fall under the umbrella of like good corporate hygiene as it relates to liquidity? Like what should CEOs actually be doing when we say, Hey, pay more attention to cash and liquidity?

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Nicholas Andrews 22:01

Yeah, I think, for me, you'd want to just, I would communicate, one, just make sure, make sure the key people and key players know, the items that are important to the business. So maybe monthly burn rate, or specific client information that is pertinent to units across the business line, so you basically don't want to have, you know, one silo or even just like one person in your business, maybe not just knowing why something might be unique to another part of the business. And I think, you know, the other side of like, would be good corporate hygiene would be, when you're tying goals and performance metrics, like tie them in. So if you have a sales manager that's got a growth, you know, you've got to achieve, you know, 5% growth in your sales this year versus last year. Also tie in the collection side of things. So don't just make it a 5% growth. But you know, maybe it's 5% growth and ensuring that we are collecting all of our if our terms are net 30, making sure we're collecting on our net 30. So tie it to a growth, but then also tie it to like a collection metric, because then you start to engage someone of okay, I'm hitting my sales target, but is the business really better off by me hitting my sales target, if our collection just keeps slipping, slipping, slipping. And if they're managing both growth and the balance sheet, I think you start to have a more holistic picture. And people are making decisions with a broader scope in mind. And I would do the same thing on down. I always have that with, you know, your purchasing manager, so managing the purchasing and in the purchasing decisions, but then also managing your days of inventory outstanding. So managing that and making sure you're adhering to what you want from a sales and operations planning standpoint.

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Steve Divitkos 23:49

That's great. I remember one practice that I engaged in, was daily monitoring of my cash balance. So every morning, the first thing I would do is log on to my online banking platform and look at the cash in and cash out over the past 24 hours. And this might sound a little bit off the fairway, but one of the things that we ended up doing specifically with our finance and accounting group that ended up kind of working, is we would turn a goal into a game. So what I mean by that is, within our finance and accounting group, I'll just make up numbers here because I don't remember exactly what they were. But let's say that our average days outstanding was 35. Well, we would give them a goal and say by end of quarter, we want to get this down to 30. And we turned it into kind of a hokey game. We put a big, colorful billboard outside of the CFOs office, we would update it every day to the extent that it went down we would do like a big cheesy celebration. I made it visible we made it fun. And it was surprisingly a very, very simple tool like that was surprisingly effective. And for anybody listening, there's two great books that talk about gamifying, for lack of a better way to put it, very specific goal like this. The first is called *The Four Disciplines of Execution*. And the second is called *The Great Game of Business* by Jack Stack, we will link to both of those in the in the show notes. But, Nick, for whatever it's worth, I had a lot of success doing really, really simple solutions like this and turning it into a bit of a game or a competition. And in my experience, as I'm sure is the case with with yours, what gets measured, tends to get done.

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Nicholas Andrews 25:36

Yeah, no, I love how you guys did that with the board outside the CFOs. Office. I mean, I think tying that in just breeds engagement. And when you can see something, when you see it, it's a little bit more tangible, for whatever reason, even if that's just, you know, a psychological trick or whatever. But if you can see the number on the page 35, it's a more tangible item, and when you can see that going down, and you can see the result of that success. And what that does, it's something to be rewarded. I think anytime you can just create engagement around what you're trying to do, and in having people understand the why I think is really important. If you just are forthcoming with hey, here's what we're trying to do, here's the broader picture of this goal, we need to try and increase this collection. I think that's going to set you up for success rather than, you know, maybe keeping people siloed or maybe not giving them the why as to, you know, for what they're doing.

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Steve Divitkos 25:36

Yep. So we're gonna bounce around a little bit here. And I don't have a great segue. So I'm just not going to even bother attempting to provide one. But I want to move on to the concept of employee financial literacy. So we're getting out of liquidity. And we're starting to speak a little bit more broadly here. And this is a question, Nick, that I've asked plenty of podcast guests in the past, and I'm very curious to get your take on it. Because if you were to survey 100 randomly selected small business CEOs, you would get a wide range of answers on the following question, which is, in your opinion, how much financial information do you think CEOs should be sharing with their entire employee base? And why?

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Nicholas Andrews 27:15

That's a great question. I come from the standpoint of, if there's something going on in the company, a strategic milestone they're trying to hit or something going on, such as liquidity crunch, I think sharing the information, sharing what's going on, and then also the plan. So you know, one of my non negotiable items is if somebody comes to me with a problem, come to me with a solution or an idea of potentially how to fix it. But when it comes to like sharing information with teams, I think sharing what's going on, what we're trying to do to either achieve that goal or fix a problem, and maybe the path forward will help elicit some understanding of what we're trying to do, and then get feedback and buy in from the people that you need to help you execute. I was actually just talking to someone recently about just kind of managing AP, you know, for one of the people I'm advising that's in a bit of a liquidity crunch. And I was just talking to them about just basic, you know, are we paying our bills on time? Are we paying them early? And what's the impact of that? Just that one conversation, you can see the light bulb go on? Oh, well, if I'm paying this early, this is actually having a negative impact on the company, I shouldn't do that. So I'm of the mindset of sharing what we're doing, why we're doing it, and then getting buy in from the team. And I think that's probably the best way to achieve the goals.

**S****Steve Divitkos 28:47**

Yeah, you know, I tend to be of those 100 randomly selected CEOs, I am probably on one of the far ends of the spectrum, and more specifically, I would advocate for full transparency. Which is to say, give them everything, every financial statement, every metric, everything unblinded. Now, I don't know if that's the right approach for all companies. I'm sure there are plenty of circumstances where that wouldn't be the case. But just for the sake of the discussion, I'll share my experience. And I'm curious to get your reaction to it. The first couple years of running my company, I actually I did not share all the financial information. In fact, I only shared revenue with people. And the reason why I did that at the time is I was frankly, just scared. I was worried that, hey, if the employee see let's say, we're too profitable, well, they're all just going to, you know, ask for raises, for example, or they're going to say, well, we should absolutely invest in resource A, B or C because we can afford it. On the other end of the spectrum, we weren't profitable enough, then I was scared that, you know, employees would start polishing up their resumes and they would get worried that the company you know, wouldn't be able to make the next payroll run. For whatever it's worth, I'll just share with everybody listening that none of those things ever happened. None of those, neither of those worries ever manifested in both good and bad periods. I think as the years progressed, my philosophy kind of turned into one that said, if you treat people like adults, they'll tend to act like adults. And if you treat people like children, they'll tend to act like children. And in my experience, A, my employees appreciated the transparency, whether it was good or bad news. B, I learned that people appreciated being trusted to solve a big problem. So the problem that I thought would prompt each of my employees to polish up their resumes, actually, they viewed as kind of a call to arms saying, hey, it's pretty cool. He trusts us to help solve this problem. And then lastly, came to learn that if you want your people to help you get to a certain destination, how can they possibly do that if they don't really know where they are relative to that destination? So my inclination is just rip off the band aid share absolutely everything. And my guess is, almost none of the things that you were worried about will end up happening. Now, again, I don't know if that's appropriate in all circumstances, in all situations, like, have you ever seen that backfire? In your experience? Or do you have any pushback against that?

**N****Nicholas Andrews 31:29**

Yeah, I don't, I'm with you in that camp, I'm always of have more information than less. I feel in scenarios when it's you have asymmetric information, it puts people at a detriment. And you need engagement to help achieve your goals. And it's tough to do that when you don't have all the information at hand. Now, you know, it's not like, you're going to tell them yourself, like, you can share every single little detail. But if we're setting up goals or metrics, you know, I communicate those or I would communicate those, you know, fully. I think, the messaging and how it comes across as what, you know, either makes people a little nervous, or if it makes people like, okay, let's roll up our sleeves. So, I think I would balance how I do the messaging, maybe, when maybe the only thing I would maybe add to that, but I'm in your camp, I want to give people all the information because they might know a blind spot that you might not see if someone's done in the details, doing something or someone might know something specific to a certain customer. And they might not feel empowered, because they haven't been given all the information to feel empowered to come, to bring the information backup. So I think I would use transparency to build engagement. And that's how I usually would go about it.

**S****Steve Divitkos 32:51**

Now I can imagine a situation where somebody listening would say, Okay, well, that's great for you guys. But for reasons A, B and C, I can't or won't do that in my business. So let's assume that somebody listening to this says that they are unwilling or unable to rip the proverbial band aid off and share everything. Okay, if they're not willing or able to share everything? Are there any metrics or pieces of data that you think everybody in the company should understand? So asked another way, if we're not going to show them everything, are there a handful of things, at the very least that everybody in the company, from the receptionist to the CFO should have a really clear understanding of?

**N****Nicholas Andrews 33:38**

Yeah, I think everyone should have a clear understanding of the policies. So that way, you know, everyone acts the same. So they, everyone knows what the policy is, I'll just use like an AP processes and example. If our terms are, you know, net 30, everyone should know, our terms are net 30, unless there's some contractual agreement there. But if we know if this policy is what it is, we should be adhering to that. And so from knowing what the metrics are, like, I would say that, you know, base level performance metrics in the business, maybe sales, growth, working capital management, everyone should know, those and know are these either in line with our goals for the year or our policies as a company. And if they're not in those that empower someone to say, hey, we always do we do net 30. And we didn't do that net 30. Why? I mean, it empowers it to stop at that certain level, you can start to head stuff off before it becomes too late. So I think knowing, you know, what the what the overarching goals are, what the overarching plan is for those for the company. So as I mentioned earlier, if it's sales growth, if it's customer growth, product growth, you know, understanding what those are and then understanding the metrics that governs those policies, I think everyone should know those from the CEO down to the frontline person

**S****Steve Divitkos 35:01**

So we've been spending a lot of time discussing sources of cash or generating cash, let's talk about the opposite side of the coin, which is actually using that cash for spending it. And capital allocation is a subject that I think is discussed in a great degree of detail with much larger companies, specifically publicly traded ones. But it's something that is, in my opinion, drastically under discussed and not particularly well understood in small and medium sized businesses. So once the business has generates cash, naturally, they have to decide how to use it or how to allocate it, they could repay debt, they could pay dividends, they could acquire other companies, they could reinvest in any number of areas, within their existing operations. Specific to small and medium sized businesses, Nick, have you seen maybe common mistakes or common oversights or common areas of misunderstanding specific to the discipline of capital allocation?

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Nicholas Andrews 36:05

Yeah, I think, kind of two come to mind. And I would say, the first is, you know, when a cash is generating business, or we're having good years, there can be a quickness or maybe a rush to maybe pull cash out of the business. So I'm a small business CEO, I had a great year, and I'm gonna pay myself a huge dividend or something or pay me and my three partners, a huge dividend. Maybe that year was a one off a one off year because of, you know, some macro economic event. So, you know, I think there's a mistake that can be made, as you know, pulling cash out of the business without maybe looking forward, or maybe understanding maybe why one year was better than the other. I think the other kind of common mistake can be once you've been generating cash is, you start looking at, hey, let's reinvest this in the business, I maybe want to build a new warehouse, or I want to build a new line. And there's not really diligent analysis done around maybe the NPV that those projects will either four or excuse me, the NPV around what those projects will generate. And then, say, there's three or four projects, there's no maybe ranking as to like, maybe which one has the highest and best use. So sometimes they become like pet projects of, hey, we had a great year. And I really want to just, you know, I really want my office to be a really, you know, awesome office. So I'm gonna reinvest capital and buying expensive furniture, for an extreme example. So I think those are, you know, kind of the common mistakes, it's a rush to pull cash out of the business and then to it's reinvesting cash back into the business, but not doing the analysis around, you know, which projects might be your highest value and your best use of your dollars.

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Steve Divitkos 37:48

Yeah, I totally agree specifically, with that second point, I found that in my experience, the two biggest like mistakes, if I can use that phrase are one, you don't measure the return that you're going to get on any particular use of cash. And to even if you do measure it, the second order mistake is you don't compare that return to other potential uses of that cash. And you mentioned NPV, as one metric, I would agree with that. And add to it the concept of a simple IRR, for example, internal rate of return. And in my experience, and my goodness, I fell into this trap, I can't tell you how many times. The biggest area for me that I had trouble with visa vie capital allocation, was hiring. Because in my experience, it's very easy. And I've written about this, it's easy to kind of throw bodies at problems, it's easy for your head of sales, your head of engineering, or head of marketing to come into your office and say, hey, my team is swamped, we need more bodies. And if you're in a highly cash generative period, it's all too easy as a CEO to say, okay, you know, you in our budget, you can hire another body. But what I didn't do a good job of is trying to quantify the return that I would get on that hire. So for example, if I'm hiring a software developer, you know, what am I gonna get? Are we going to release a new product that we otherwise wouldn't have released? Are we going to release an existing product? I don't know, six months faster than we otherwise would have released it? And if so, how much is that worth to the company? Right, let's say we'll get a 10% return on it. Well, that's great. But if I can get a 15% return by, I don't know repaying venture debt or paying distributions, maybe that's a better use of cash. So, for me, it's the measurement, and once measured, comparing it to other uses of that capital, and I just find hiring was really, really hard to do. I mean, how have you dealt with situations Nick, when a member of the management team comes to you and says, Hey, Nick, I know this isn't in the budget, but Team XYZ is just drowning, we need to throw another body? That happens daily to CEOs. I'm sure a lot of people can empathize with that. How have you dealt with situations like that in the past?

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**Nicholas Andrews 40:12**

Yeah, that question is a great question. Because I mean, all you have to do is just open up the Wall Street Journal right now, and I think you'll find, you know, a bunch of articles about Google and all these other companies that have for the last two years just been hire, hire, hire, and they've either slowed or stopped or laying off, you know, workers. For me, when I've encountered that when they've said, Hey, we're swamped, we need we need help? My my usual first question is why? And trying to understand why is it process is volume? What is really driving that? So I can understand, what is this? What is generating this problem, and then maybe how to attack that solution rather than just throwing bodies at it. Because, like you said, in cash rich times, it's easy just to say, well, we've got the mone, hire a person, hire a person. But then what happens with you know, the productivity, it's a short term problem, you know, we had a customer by, you know, 50% above what they normally buy. So we're just really busy for a few months, and what happens when we go back to steady state? So I first tried to attack it by understanding what's driving the problem. And then from there looking at, if we hire this person, what the steady state is going to be looking like? Because it's tough, I've always found it to be a little tough to measure, you know, kind of return. But I've said, okay, well, once we slow down, what is the steady state look like? Is this person going to have 10% or 15% of their time idle now, if we're if we go back to steady state? Or are we just on a continual growth path? Are we going to need to be adding, you know, 1.5 FTE is every year at this rate? So that's how I've usually approached it is what's driving the problem? Is it a person that's actually the solution? Or is it maybe a process change? I've also looked internally for resources, how can we maybe repurpose someone who's idle? One of my one of my clients was kind of going through this where an accounting staff needed some help. And there was a person that was kind of doing part of that job that they needed help with originally. So it was looking internally, can we just repurpose this person so that way, maybe they don't have idle time and kind of have them bridge that gap? That's usually how I've approached those decisions when hiring has been brought up.

S

**Steve Divitkos 42:25**

Yeah, and it's a lot easier to add than it is to take away as all of each of the companies that you described reading about in The Wall Street Journal this morning can attest to. In all of the questions I've been asking you, Nick, there's been kind of an underlying assumption that the companies in questions are net generators of cash, which is to say that their cash balance is deliberately and purposely increasing over time. But there are plenty of companies who are net users of cash, which is to say that they are very purposely decreasing their cash balance over time, presumably investing in some aspect of their business in hopes of a future return. Companies who have received growth equity are illustrative examples. I mean, the whole point of growth equity is to spend it otherwise, why'd you raise it? So hypothetically, if you're sitting on the board of a company, that is a net user of cash, which is to say, Hey, we are burning cash, we are doing so on purpose? I mean, what are the things that you would look at to make you comfortable with that reality? Are there unit economics? Are there payback periods? I mean, what are the metrics you look at that would get you comfortable in a situation like that? Because I know a lot of folks listening to this are running businesses that fit that description.

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Nicholas Andrews 43:45

Yeah, I mean, that's a great question. Yeah. For like for rapidly growing businesses. I mean, the items that I'd look at there would be you mentioned this earlier, but unit economics, I'd be looking at breakeven points, saying, are we at least positive on some of our, we're growing here, but what is changing in our unit economics? And how are those holding up to our assumptions and projections, as we're adding this growth? Because production costs are not linear to a point, I mean, there is the marginal rate here where it does start to change. I mean, it's linear to a point, but you start adding lines, you're gonna have these jumps, or you're gonna have changes. So for me, I'd be looking a lot really focusing on unit economics and making sure those are staying intact. And then for acquiring customers, I'd be looking at, well, what are we paying to acquire those customers versus what they're generating? Because if that ratio, depending on the balance of that ratio, if they're generating more than it's costing us to acquire, you know, that's the area you want to be in as you're growing. If you're paying more than what they're generating, that's not a sustainable path, and you can keep throwing cash at that, but eventually, you're just going to run out of cash at that point. So for me I would look at I would look for signs that you know, we're at least pause Whatever your economics positive on what it's taking to acquire customers and use that as my measure at each stage in the business,

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Steve Divitkos 45:08

At a more kind of extreme part of the example, I think of like venture funded companies now, you know, that doesn't, you know, frankly, represent a huge percentage of our audience. But to the extent that it does, and I'm the furthest thing away from a venture investor, but friends and colleagues of mine, who are, naturally look at burn rates, and basically say, well, at your current burn rate, how many months of cash do you have in the bank before you have to kind of go back to the market and raise? And we're coming out of a very, very long cycle where the default assumption with companies is, hey, you know, if we have to go to market every year to raise then let's do it, because the capital markets supported it. Now, that type of what I'll call capital market risk in businesses is totally different. And friends of mine who are in VC are advising their portfolio companies, hey, you should have upwards of two, maybe even three years of cash on your balance sheet now, so decrease your burn rate to ensure that you're kind of default alive for the next three years. Which is probably why you're seeing so many layoffs happening in the venture funded world. And for companies who are, you know, burning cash, or at least kind of, let's say, cashflow, breakeven, it's just something that I would encourage folks to take a look at, which is to ensure that there's a lot of risks in every business. But to the extent that you can, remove what I'll call capital markets risk from your business, because it's just impossible to predict. And it certainly looks like we're going into a slowdown, where you can no longer set your watch to the fact that you can just raise money next year.

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Nicholas Andrews 46:47

Yeah, yeah. Yeah, it's a pretty interesting, pretty interesting time with, I'm not in VC, I can only maybe just speak to kind of my thoughts. And what I've seen, but yeah, I mean, you're exactly right. The I think the venture backed companies have the ability, you know, if I'm raising 12 months of cash, and it takes me three months to do my raise, so I'm gonna start raising in nine months, they can almost set their watch to it. I'm going to go out, raise money, raise money, and I'll have my next you know, 12 months, 18 months, and outside looking in looking at those environments, you know, seeing that those venture backed companies that basically have just been said, you know, how can you increase your burn rate? Maybe, you know, can you reduce costs. And one of the items that I thought was interesting was one, venture backed company was told by their partner, you know, maybe you could look at reducing staff to reduce your burn rate, and not just cutting headcount, but just cutting hours. So maybe your days, four days a week versus five, so there's 20%, decrease in your burn rate. So, you know, it's kind of just interesting, you know, levers that you could pull. But yeah, it's fascinating to see what's going on in that market, and how those runways now are being extended, and how CEOs are having to look at or founders are having to look at how they can increase that runway.

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Steve Divitkos 48:08

Yeah, it's something that a lot of companies, including my own, had to do the early days of COVID-19, you know, four days a week instead of five, that's a 20% reduction to burn rate, right their. Salary reductions, which is, you know, of course, you have to be very, very careful in pulling that lever. But we had to do that, plenty of other businesses had to do that. So there are levers that you can pull beyond layoffs. But Nick, not to put any pressure on you. But the following question is the question that I was most excited to ask you. So if I had a drumroll, maybe I can edit it in, but it has to do with budgets. The reason why I want to ask you this question is because the I found as a CEO, we'd spend months producing a budget. And then, in any given year, it probably took only a couple of months for things to quickly change. Things happen that were completely unanticipated. And our budget quickly felt like it became meaningless in spite of all the work that we put into it. So you know, on one hand, you want the discipline that a budget creates. But on the other hand, you kind of need the flexibility that the real world demands. Yeah. So can a 12 month budget do that? Is it even possible? If so, how? And if not, like, are there other tools other ways to look at it that can balance you know, the requirement for both discipline and flexibility that I just found a 12 month budget never provided me with?

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Nicholas Andrews 49:48

Yeah, that's a common sentiment that I've heard about, you know, we spend all this time to put together this budget and then it's meaningless after February 28th. Yeah, I'm with you, I like the the foundation that putting together a budget provides. Anytime I'm involved in, you know, the budgeting process and thinking about that, you know, the the numbers are important to me, I really focus or what I keep on on my mind is the underlying assumptions around maybe sales growth or customer acquisition. The assumptions around maybe working capital management or changes in that, and then the capex plan are the items that, you know, I kind of keep in the back of my mind. So, I like the I like the discipline that the budgeting process

creates. But I also try and be nimble with how I go through that process, knowing that it's going to change and probably be obsolete by the end of one cue. So where I've usually focused on as brief forecasting, so, you know, as we as you hit, so let's just assume your calendar year and company, you've done your budget for coming up, starting in January. You get into January, you get into February, I'm always looking back to actuals, versus the assumptions, not necessarily the budget, but I'm looking back to assumption. So if we've said, we thought, you know, this would be a 5% growth or a 10% growth in the first like, two months, did we hit that yes or no, and why, and then looking at what the downstream impacts that might be for the rest of the year, and then start to build out, you know, re forecasting. And for me, that usually starts around the first quarter, looking at the first two months of the year, first few months of the year, seeing how we've done, and then building out a forecast. And it seems like things are changing so quick, you know, it's not uncommon to be doing six month forecasts, or doing maybe even like a six month budget. But I tend to look at reef forecasts as being a little more powerful than trying to recast the whole budget, I look at maybe what's changed and use that as a model to say, Okay, this part of what we did do for the budget is still intact, this part has changed. So let's use the part that's still intact, let's use the part that's changed and do a re forecast, and then start running that against our base level assumptions. So, maybe our sales have slowed, well, did our collection stay intact? Are we still collecting on the right place? Because if we're still collecting on the right pace, I know that you know, my cash forecast, and I'm doing a cash forecast that can at least hold. So if maybe my sales slowed, and maybe my cash collections show slowed, I might need to adjust how many be how much cash, I need to keep in reserve on the balance sheet. So I kind of use those items in tandem, as I think about budgeting and forecasting as we move through the year. And then by the time you get to September, October, you have a pretty good idea of how things are shaking out. So one of the things that I toyed with but I never actually did was instead of an annual budget, do a six month budget, or maybe even just do a quarterly budget, in an attempt to kind of strike that balance between discipline and flexibility. When you say you're a fan of the reforecasting method, can you just contrast that with let's say, doing a three or six month budget? Like what what what is the difference between those two strategies? And why do you prefer the reef forecasting method. So, you know, I would prefer it, when I when I think about doing a budget, I think about that completely bottom up every single variable that goes into it. And with with re forecasting, maybe you might not have to do that. Now, if you have to re forecast everything, you're basically just doing an entirely new budget. But if only certain, you know, maybe lovers or certain items are changing with what you had originally budgeted, you can do every forecast and layer in your budget items. And then evaluate to see how maybe gross margins have changed or how maybe certain EBITDA has changed, you know, kind of looking at looking at metrics. To then maybe say like, okay, maybe we do need to do a completely revised bottom up budget, it's changed that materially that we need to do a revised budget. So you know, when I think about a budgeting process, to me, that's every single line going through every single piece in the in the financial statements, and you might not have to do that. Now, it might vary across businesses, or if there's macro macro factors playing into maybe certain industries. So I wouldn't say that you should only do one or the other. But, you know, re forecasting might provide you a little bit more flexibility in how you look at your numbers and maybe time. But if you're having to rebuild everything every quarter or every six months, if the business has changed that much, it's probably something you're gonna have to do just to you know, make sure you meet your goals and objectives.

**S****Steve Divitkos 54:48**

Let's pivot into another set of questions that have less to do with liquidity but are certainly on the minds of CEOs as it relates to the finance and accounting function. And I'm talking specifically about hiring. It is not abnormal for a smaller, medium sized business to be meaningfully under resourced in the finance and accounting group. Sometimes it is the founder herself doing the books, sometimes it is a spouse or a family member, sometimes it is outsourced to an external party. But in many, many, many instances, it is under resourced and often underperforming. So for that reason, lots of CEOs have to hire in a finance and accounting leader effectively for the first time. So let's presume that you know, we're CEO, and we're in that situation, we're looking to hire in a finance and accounting leader, whether it's a controller or a director, or VP of Finance, whatever the case may be. Maybe just a couple of questions, assuming that that's the world we're living in. The first is, in your opinion, what is the difference between, let's say, hiring a CFO versus, let's say, a VP or director of finance? Or is there a difference?

**N****Nicholas Andrews 56:11**

Yeah, so short answer is yes, I think there's a difference. And it really just comes down to, you know, what that person has done maybe in their career, who you're bringing into that role. But typically, when you think about, you know, CFO versus the VP or director of finance, the CFO should really be viewed as your strategic partner. So we've got goals of where we want to be, how do we achieve those in an efficient manner? How do we evaluate the capital structure the business? How do we evaluate the, you know, capital expenditures of the business, you know, to meet the growth targets. So really, like the CFO is really the, I would say, the strategy side of thing. Where a VP of Finance or director of finance, that's going to be someone who's going to be more day to day down in the weeds, so to speak, you know, they're going to be compiling the budgets, compiling the forecast, maybe putting together the underlying data, but more focused on nuanced details that are needed in order to complete maybe financial projections or financial analysis, that would go into decision making. So when I, you know, when I think CFO versus like, VP, finance director, finance to me, I think, strategic forward looking view versus day to day down in the weeds view.

**S****Steve Divitkos 57:33**

I had a previous director of finance, who asked me a similar question. It was in like a career progression meeting. And he kind of asked me to differentiate between his current role which at the time was a director of finance and his desired role, which is, at the time was the CFO. And I have no idea if this is a correct or even reasonable explanation. But what happened to come out of my mouth at the time was, you know, I think about a director of finance as a talented accountant who works in a business. But I think about a CFO as a talented business person who happens to be really good at finance and accounting. Yeah.

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Nicholas Andrews 58:11

Yeah, I think that's a great, I think that's a great way to sum it up.

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Steve Divitkos 58:15

So how does somebody know what they need? So again, this is a CEO who's making this hire for the first time? How does she know as a CEO? You know, do I need a controller? Do I need a director of finance? Do I need a VP? Do I need a CFO? Other than the qualitative differentiation that we just provided? Are there other things you should look at? So for example, I don't know revenue thresholds, profitability thresholds? I don't know employee thresholds? Like, how does she know what she actually needs?

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Nicholas Andrews 58:48

Yeah, when I think about, like building out a building out a finance function, I think you need someone you need to have strong accounting, one. So you need whoever's doing the day to day accounting, you need to have that person there. So when I think about a structure or an organization, the person doing the numbers needs to know that forwards and backwards, so like, I think you need a controller or you need an accounting manager controller, you know, whatever, you want to kind of title them there. But you need your base level accounting to be correct, because if it's not, then it doesn't matter what you're doing from financial projections and what and go forwards. It's just, it's not going to work. So, I think if you if you're looking at the finance function, it's like, do you have that base need met? And if you do, then, you know, do you have that strategic growth partner that you need in the business? And if the answer is no, then I would say you're going to need to bring in someone who can think strategically. So to me, that is that is a CFO role at that point, or you know, even if it's on like a fractional basis. You know, because you're you can use a controller role to maybe hybrid and put it together some, you know, financial projections. or some financial modeling for maybe projects. I mean, those models aren't that difficult to build. But really, if you're looking for a strategic partner, kind of like you said, a business person who's really good at finance, that's when I would say you need to probably bring in a CFO, if you're looking to grow the business, but how to tie in the numbers, that's when you need a CFO.

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Steve Divitkos 1:00:23

And so even more tactically, when we are hiring, whoever this person is, whether it be a controller, or CFO, or anywhere in between, what specifically in your experience should CEOs look for in both the interview process and the resumes? And I guess, conversely, are there any maybe red flags that CEOs should be aware of that might be suggestive of potentially making a bad hire?

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Nicholas Andrews 1:00:49

Yeah, you know what, anytime I'm looking to fill a role or, you know, interview someone, the more senior it gets, the more I look for, I look for people who, you know, did something. And what I mean by that is, maybe drove change, I saw a problem, and here's what I did to fix it, or I saw an opportunity to make this change and help the business grow. So as the more senior the levels are, those are the types of items that I that I look for, because back to what you said is earlier, like how you phrased that with, you know, a good business person who knows finance, the more senior that that role needs to be, the more you need them to be able to think strategically. And so when I'm looking at resumes, so if it's a CFO role, or a VP of Finance role, that's what I'm looking for in that candidate is what they've done, I looked for base level experience, base level education, but really, what did you do in your roles? Were you just coming in and pulling a lever every day? Or were you actually thinking and what was challenging? And so usually, when I'm talking with them, I'm asking questions, you know, what didn't work? Well, and what did you do to fix it? How did you lead through, you know, what adversity did you face? How did you navigate that? Because, you know, if everything was just, you know, cherry and gumdrops, then it's not you need some type of adversity to understand, you know, how to manage through tough situations. So I'm looking for someone who's who's done difficult, you know, either hiring or making product decisions, or looking for for growth opportunities, or business acquisitions, just I'm looking for someone who's who's had to think outside the box and had to operate maybe an ambiguous situation. So the more senior it is, that's what I look for. When when you step down into like, maybe technical roles, like accounting or, or like a director of finance, for them looking for specific technical knowledge. So on the controller side, I'd ask them about specific accounting standards that relate to your business, you know, if you're a SaaS based business or subscription business, you know, ask them about the accounting standards for it, 606. How do we how do we handle our revenue recognition? How do we, you know, how do we handle leasing standards? I mean, that's kind of a big one, and what effects maybe do those have on my business, if we haven't implemented those and have have that person kind of talk you through it, what the implications are? Because if they can assess the technical standards, and they can explain to you how this is going to affect maybe your business, if you haven't adopted those standards, that's a good person to have. And if they can't, that's a red flag and probably should avoid them.

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Steve Divitkos 1:03:37

At the risk of going on a tangent, the answer to the first part of the question, which is, you emphasize, Hey, what did you actually do in this role reminds me of, frankly, my biggest pet peeve when it comes to reading resumes. And the pet peeve is the difference between like, what did you do in your job versus what did you accomplish in your job. Way too many times, and frankly, more often than not, when I read resumes, it reads like a job description, right? It tells me like what you did, and like, you know, at the risk of saying it, I don't really care what you did. That's what you get paid salary for. And that's what any person ought to have done in that role. I'm much more interested in like, what did you accomplish in that role? And so maybe I'll take this perhaps inopportune opportunity to air my grievances as it relates to all resumes and suggest to everybody that if you've got a resume that reads largely in the spirit of what you did, please erase it and please rewrite it in the language of what did you accomplish? Because it's then left to the interviewer to kind of tease that stuff out. And gosh, I wish it was just written on a piece of paper in front of me.

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Nicholas Andrews 1:04:54

Yeah, exactly. Yeah. And I mean when I read resumes like that, that's you can kind of separate them from people who have actually done something in their roles or been challenged in their roles versus someone who just came in, I came in, I did the minimum of what was expected to me, it was five o'clock, I walked out the door, and I didn't think about it anymore. Yeah, your pet peeve with that is my exact pet peeve. I will read resumes with a highlighter and all, maybe just highlight one or two things and just say, like, explain more about this, if I see accomplishment, and if I just see, you know, I process this, I did my monthly, I did my capex, you know, capital plan where I did my MPVs. And then that's it, you know? Yeah, I just pass.

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Steve Divitkos 1:05:42

It's not compelling, right? I mean, I could have just read the job description.

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Nicholas Andrews 1:05:45

Exactly. I could have read what was asked of you and understood that you just did that, what was asked of you.

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Steve Divitkos 1:05:50

So let's put my very specific pet peeve aside, let's say that we have hired this person. How do you know that a newly hired finance or accounting leader like how do you know they're doing a good job? Are there any metrics that you look at? Are there any milestones that should be achieved within a certain period of time? Like, how do you inform the question of whether this new hire is actually doing a good job?

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Nicholas Andrews 1:06:16

Yeah, I'm looking at how well they can speak about the business. So if they've stepped into this company, they're new into the company, you know, do they really understand the nuances of what makes it tick? That's what I look for just number one. So I look at for how they talk about things. And then how, you know, if they're talking about specific items related to the business, I look at how they talk about potential changes, and what that would do if we have these, you know, if someone came to me and said, Hey, we have 10 customers, but two of those customers represent 80% of our sales, that they come to me with some like quality analysis about some nuance in the business. That's what I look for. If, after a certain period of time, you know, they haven't really brought any type of analysis or added any type of, you know, specific knowledge or maybe something they're seeing in the industry or the market. That to me is something that might stick out that maybe they're not really taking full command of their responsibilities. And what they've been hired to do.

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Steve Divitkos 1:07:19

Is it to kind of mechanical and robotic to hold people to quantifiable standards. So two things that just kind of immediately came to mind. I just wrote them down so I didn't forget them. As I was brainstorming, but what would these metrics actually be? Can you hold a newly hired let's say, they've been in the job for three months for example, can you hold them accountable for things like days payable? Days receivable? Can you hold them accountable for Hey, you know, we expect the books to be fully closed, X weeks after month? And like, is that too mechanical and robotic? Or it's just holding people accountable?

N

Nicholas Andrews 1:07:57

No, it's not, and those items should be put in place. So if you're, I'll just kind of pick the one. So you mentioned, like closing the books. So if you haven't, so like, let's just assume you've got an issue, getting financial statements out on time. So you've hired a new CFO overseeing the finance function, said, Hey, we need to have the books closed by day five. This is an example. So I think it's perfectly reasonable to say, this is now what I'm holding you accountable to. But I think I would follow it up with giving them the mandate and the power to enforce that. So if it's a people process or systems issue, giving them the power to mitigate that, so that way they can achieve that goal. So I think it's perfectly reasonable to hold them to whoever you bring into that role, hold them to targets, but then also give them the mandate and the power to achieve that. Because if you don't give them the mandate or the power, they can't achieve that goal. And you've really you've kind of just hamstringing that position a little bit. But no, I think having quantifiable goals and metrics in place is perfectly reasonable, as long as they're coupled with the mandate to to achieve those goals.

S

Steve Divitkos 1:09:06

Yeah, and I guess the one thing that you are suggesting, but maybe I'll just say it more explicitly, just for the sake of doing so. If you're holding people to numeric or quantitative standards, they should know what the standards are on day one, right? So the day that you hire somebody, you got to say, hey, you know, we're expecting you to work towards a monthly close within X weeks, or we want our payables to or pardon me our receivables to decrease by X percent. I mean, you can't have a difficult conversation four months into the job and say, Hey, we're holding you to all these standards. And hey, by the way, here are all those standards for the first time.

N

Nicholas Andrews 1:09:44

Yep, yeah, no, no, that should be a day one conversation. This is what clearly what we need, you know, this is clearly what you're being hired for. Now, here's how you can go execute it and I'm empowering you to go out execute it. So please come back to me with what's not allowing you to achieve this goal.

S

Steve Divitkos 1:10:06

Okay, Nick, as we look to wrap up here, there's a lot going on from a macro perspective. That's how we started our conversation today, the war in Europe, interest rates, inflation, your dog barking, all these kinds of uncontrollable things. With regards to all of these things that are happening, that are outside of the CEOs control, is there anything tactically speaking that CEO should be doing in light of what's happening from a macroeconomic standpoint, that we haven't already discussed today?

N

Nicholas Andrews 1:10:45

I think the other item that maybe CEO should look at is, you know, the inflationary environment right now is just unprecedented, you know, as we discussed earlier not in 40 years has it been this high. But I think, you know, one of the items to consider is, you know, as the Federal Reserve is adjusting to this, or as central bankers are adjusting to this inflationary environment, there's an interest rate change that is going on. And so I think what CEOs need to look at is maybe how their cost of capital or their weighted average cost of capital has changed in this in this inflationary environment. So if the use of variable rate debt is being used as a component of that company, there's likely that that variable rate debt is being reset on a quarterly basis. So understanding how that is changing, because if your cost of capital is increasing from a debt and equity perspective, you need to make sure that you're accounting for that when you're looking at maybe capital decisions and underwriting to maybe new hurdle rates or higher hurdle rates. So that way, you know, maybe you don't take on a project that is now negative NPV or negative IRR, you know, if it's a negative project to your company, under your current cost of capital, whereas, you know, in your previous number, it might have been a project that was a go. So I think just understanding how the broader interest rate environment has changed and how that affects the cost of capital, is what I think CEOs should maybe just keep an eye on as they go forward.

S

Steve Divitkos 1:12:24

That's great. Very, very insightful. Nick, you've been very generous with your time. We really appreciate you lending your insights on all things finance and accounting, from hiring to working capital and everything in between. Thanks so much for being generous with your time and we really appreciate you joining the show today.

N

Nicholas Andrews 1:12:45

Thanks for having me, Steve. It was great talking with you and I hope it was useful.