

BUSINESS STRATEGIES ||| BY CHUCK YENKNER

Buying capital equipment

Exactly what is capital equipment? And what is the difference between buying capital equipment versus other purchases made for the lab?



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Let's start off by defining

the term "capital equipment." In "accountant-speak" capital equipment is "equipment or machines used to produce products." In our case, that means equipment such as furnaces, boil out tanks, benches, and those new CAD/CAM milling systems. Capital equipment, unlike consumable products, is not used up in the production process but rather eventually wears out, depreciating in value each year. Most companies set a dollar limit to indicate at what cost a machine is considered capital equipment opposed to a one-time expense.

The reason capital equipment is such a hot topic in our industry today is because of the increasing cost and complexity of the machinery currently on the market. Large capital equipment investment is being driven by patient and dentist demand for stronger, more esthetic, more biocompatible, and in some cases less expensive prostheses. Add to the mix a shortage of trained technicians and the result is \$150,000 equipment systems that can take over some of the lab processes once done by hand.

WHEN TO INVEST

As a lab owner or manager, you need to be smarter than ever about buying capital equipment. The potential financial impact on your business if a bad purchase decision is made has grown exponentially. The wrong decision on a \$3,500 porcelain furnace is not good but it probably won't

put you out of business. However, the stakes get much higher when considering purchase of a \$100,000 CAD/CAM system. The most common question I get in my consulting practice is, "When should I invest?" My answer is simple: "You should buy a new piece of equipment when that equipment can be run a sufficient number of hours to produce the required revenue to pay for itself." Take a look at the Capital Investment Calculator below to help you figure out your investment strategy.

In this case, the table tells us that roughly 1000 units must be produced to pay for the

margin on the new product.

Let's say your lab can sell 25 units per month of this new product and not cannibalize any existing sales. It would take 40 months (3.4 years) to make back the \$100,000 investment. (I'm not considering financing costs here). At 50 units per month the payback becomes 20 months (1.7 years). In this rapidly changing industry, I recommend not buying a piece of equipment unless you can pay it off in less than 3 years.

OTHER OPTIONS

For technologies as expensive as CAD/CAM, it usually is a smart practice to start by outsourcing your copings. This allows you to test-market the product without the risk of a large financial commitment and also accurately estimate how many units you can sell. When sales build to an acceptable break-even point, then you can purchase.

Leasing is also an option. Leasing frees up capital that you would otherwise spend on a new piece of equipment but it does not lessen the risk you take. You still will be responsible for monthly lease payments over a specified period of time.

My advice. Talk to your business advisors and accountant to construct a calculation table. The results won't tell you what to do, but they will give you the facts and the foundation upon which to make a sound business decision.

CAPITAL INVESTMENT CALCULATOR

New Capital Equipment Cost	\$100,000
Selling Price of units produced	\$200
Cost of Goods (Material, Production, Labor etc)	\$70
Indirect costs (Lab Overhead)	\$30
Profit Margin for units produced on the new equipment	\$100/unit

\$100,000 purchase price. The question now becomes, how many hours of machine operation will it take to produce the 1000 units and how many days or weeks will it take you to sell 1000 units? Keep in mind, for standing customers who switch from buying existing products to purchasing this new product, you must deduct the profit margin on existing sales from the profit

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