

DATA DRIVEN, A/E STRATEGIES FOR SUSTAINABLE SUCCESS

IF YOU FOUND \$48K ON THE GROUND, WOULD YOU PICK IT UP?

Brian Flynn, P.E., BCEE, author of *Maximizing Engineering Firm Profits—Profit Fundamentals*

Usually consulting firms make a profit, and in doing so, generate cash. Most firms clear out the cash drawer at the end of their tax years—employee bonuses, owners' distributions, investments in equipment, and some retained earnings. Then, the cash builds up during the subsequent year and disappears again.

So, how do firms invest their accumulating cash? In many cases, it sits in their checking accounts, earning virtually no interest. Why? Because we have been lulled to sleep by virtually zero short-term interest rates in the aftermath of the Great Recession. But, for the past several years the Federal Reserve has steadily raised short-term rates as a constraint against future inflation. If you have not awoken to the implications of this, it is time to do so.

KEEP AN EYE ON RATES

In December of 2008 The Federal Reserve set the target range for the federal funds rate at a record low of zero – .25 percent. Since 2016 the rate has increased to 1.25 – 1.5 percent at the start of last year, and raised 25bps four times from then to now. We are now at 2.25 – 2.5 percent. By contrast, a typical checking account remains stuck at close to zero percent: .05 percent.

What to do? Look at some of the alternatives in the enclosed table. Obviously, you do not want to play fast and loose with your firm's cash. Higher interest must be moderated by low risk. You want your risk-to-principal to be very low.

Imagine a simplified situation where a firm has \$20 million/year in net revenue, is earning 20 percent return on net, and is realizing virtually all of it as cash. In the beginning of the year, there is a zero balance; at the end,

\$4 million. The average balance is \$2 million. If you can obtain 2.4 percent versus almost zero, you will earn \$48K in interest with very little effort.

How much interest do you currently earn on your cash? Let me know. Email me at bflynn@psmj.com and tell me the interest rate you are getting. I will report the average and range of the results. No firm will be identified. ■

SHORT TERM INTEREST RATES MID-JANUARY 2019

Financial Instrument	Approximate Interest Rate (%)
Bank Checking Account	0.05 *
Bank Savings Account	0.30 *
Brokerage Money Market Account	2.30 *
Ultrashort Bond Fund (Vanguard)	2.23 **
1 Year Bank CD	2.70 *
1 Month Treasury Note	2.40
3 Month Treasury Note	2.42
6 Month Treasury Note	2.51
1 Year Treasury Bill	2.57
30 Year Treasury Bill	3.04 ***

* No risk to principal if account is below FDIC insurance limit

** Small risk to principal based on approximate duration of 1 year

*** Added for reference to illustrate shallowness of yield curve