The POWER of Reinvesting in Your Dental Practice

by Eric J. Morin, MBA

Your dental practice is truly one of your greatest sources of wealth, the key is to learn how to invest in it properly. Corporations are aware of the strong return, which is the reason so many of them are trying to enter the industry. Dental practices traditionally offer a high rate of return and very low risk, which makes reinvesting in your practice ideal.

The key to success in investing is to truly understand the numbers and how to calculate ROI (return on investment). As a dental business owner, if you can learn how to quantify the results of your investment and put those dollars to use, you can reach almost any financial goal you are working towards.

Return on Investment

One of the first things doctors must do as business owners is to identify areas that matter most. I find that when doctors are trying to make decisions about spending or reinvesting in the dental practice, they often evaluate the cost and interest rate. In business, most individuals are cost focused. They spend most of their time focused on what something costs, instead of focusing on what is most important, the potential return on the investment. I rarely find dentists calculating the overall rate of return of an investment, even though it should be the most important determinant.

The power of understanding the return on your capital investments is significant to the growth of your practice and your overall wealth. Doctors often assume that if they received a low interest rate, they have made a good decision, and if they paid a higher interest rate, they have made a poor decision. I am not saying that interest rate is insignificant, but as a business owner it is extremely important to focus on the return that the investment will bring to the practice. If you pay a 6% rate of interest, but wind up with a 40% rate of return, we would have to argue that that you made a good investment.

Debt and Equity

Another key concept to understand when looking at capital investment decisions is that we have to decide whether to use Debt or Equilty (cash):

Debt = More Risk
Equity = More Expensive

Equity is more expensive because it represents the opportunity cost of what you could be doing with those dollars. Inversely, when we look at debt, it makes us nervous. Too much debt can keep us awake at night. However, debt leveraged/managed properly and utilized correctly can accelerate practice growth and wealth. Now there is a distinguishable difference between consumer debt (personal debt) and business debt.

Consumer Debt - does not have a return on investment and is used to fund lifestyle.

Business Debt - has a quantifiable rate of return and accelerates growth and income.

I am going to take a moment at this point to address the personal home. Yes, every real estate agent will tell you that a home is an investment. I would argue that a home is an expense. I have worked with many individuals and have rarely seen someone sell their home, downgrade, and keep the cash. Most individuals roll equity into a larger home or cash out with a home equity loan, turning their equity into debt. If you are going to have personal debt, I don't think anyone would challenge the idea that your home is where it should be, but remember that the larger home you purchase, the higher the maintenance cost.

Using Debt Properly to Purchase a New Operatory

It is important to understand in this example that when we calculate your overall return on investment, we will not take into account all of your overhead. You will only incur fixed cost in the additional debt payment and the additional variable costs of any staff that need to be hired, additional supply expense and lab costs. Therefore, as you'll see below, the rate of return on the investment in which you use someone else's money is approximately 40-60%, depending on the margins. That's a good investment!

Additional Operatory

Assuming that the operatory allows $20,000 a month in additional revenue, in a year that would be ($240,000).

$240,000 X 50% = $120,000

This means that you could pay off the operatory in 6 months and have the $10,000 a month to reinvest back into your corporation. Another way to look at it is that you have now increased your take home pay, after taxes, by approximately $100,000.

Now do you want to know the real power?

If you had a million dollar loan on your building, on a 20 year note, and you applied the $10,000 a month to your loan, you would pay off you building in approximately 6 years!

You would also save approximately $430,000 in interest on the loan at a 5% interest rate.

This is why investing in a dental practice is such a great place to put money. The key is not taking 5 years to pay the debt back, but allocating the profit to immediately pay off debt.

Unfortunately, what I see most often is multiple loans on the balance sheet that sit there for years and years, taking away from cash flow and increasing personal and business debt. It also steals the ability to reinvest that capital back into the practice.

Personal Decisions Affect Reinvesting into Your Practice

Now that we have established why a dental practice is such an amazing place to invest, we must also note that personal capital decisions will come into play with not just your wealth, but your ability to reinvest back into this amazing asset. Simply put, the more money that needs to be taken home, the fewer dollars that can be reinvested back in the practice. Let's look at how a personal decision might affect this ability.

You are driving down the road with your spouse and you see THE car sitting on the rack with the giant sign that says 0% Interest. Let's assume the car is approximately $60K, so you tell each other that this is the perfect time to buy that new car that you have always wanted. You've worked hard. You deserve it. So, you purchase the car and happily call all your friends and family and tell them what a great decision you have made.

There is, however, an opportunity cost to your decision that you did not consider. Let's assume the payment is $830 on that new car that you received for 0% interest. Let's also assume that you have a 30-year mortgage on a $460,000 home at 5% interest.

Loan Principle:
$460,000

Term: 30 Years Payment
(Principle and Interest):
$2,469

Total Interest Paid:
$428,977

Instead of purchasing the car, what if you decided to allocate the same dollars towards your personal mortgage?

The effect on the loan would be as follows:

Term:
Approximately 18 Years

Total Interest Paid:
$230,095

So the Opportunity Cost of this decision is $198,882

$428,977
(Total Interest at 30 Year Mortgage):

$230,095
(Totals Interest at an 18-Year Mortgage) =
$198,882

Now we need to add back in the cost of the car, $60k, so therefore the total cost of our decision to buy the car at 0% is $198,882 + 60,000 = $258,882.

...also it is important to note that the car payment of $830 is paid with after tax dollars and it would actually cost you approximately $1080 a month.

As you can see, not only is your dental practice a phenomenal investment opportunity right in the palm of your hand, but if you make the correct decisions with your business and personal investments, it can have a dramatic affect on our wealth and ability to reach your goals. Instead of being so focused on the cost, you need to start turning your attention to the return and how to use the resulting capital.

This practical strategy will allow you to have the practice that you have always wanted and reach your wealth goals.

Claim Your Future Now

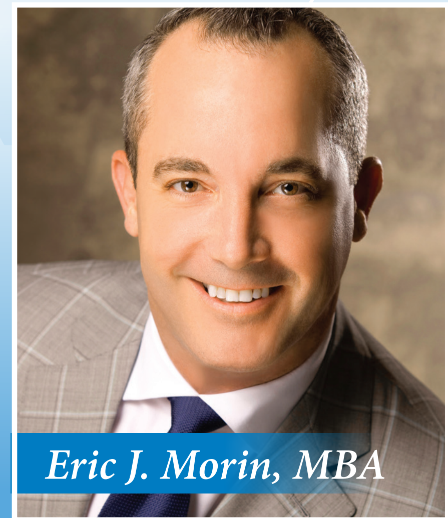
My recommendation for this year is to sit down and create a plan utilizing these key steps:

- Make a list of major capital investments needed in 2017, and decide what percentage will be funded by debt / equity (cash).
- Calculate the return on investment*.
- Create a plan of what you will do with excess capital from the return.

**If you need assistance calculating the return or how to put this into an overall strategic business financial plan please feel free to reach out to us 404-509-0452*

You will find that once you get a handle on these concepts, you will have more cash flow to improve patient experience, reduce long-term debt, decrease personal stress, and reach your financial goals at a much faster pace. Put these steps in to place, and make 2017 one of your best years ever.

When you're ready to start applying these concepts and learn more about how to grow your wealth utilizing your practice, feel free to reach out to Tower Leadership or sign up for our next workshop at www.towerleadership.com



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Eric J. Morin specializes in business and financial consulting for dentists. He has been in the industry for over a decade and also assisted his wife in establishing a thriving multi-doctor practice.

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