FACTORS THAT AFFECT OUR ECONOMY, DENTISTRY AND YOUR BUSINESS – PART II

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A couple of weeks ago, we went over some of the factors that contributed to the current situation. If you missed that, click here to read what happened. This time, we're going to explore some of the risks/problems that have developed as a result of these factors. They can be broken down into three aspects:

1. Growth
2. Interest rate fluctuations
3. Lease costs
4. Retirement for all age groups

First, there is growth. The economy is held in equilibrium by supply and demand. Supply, in this case, is the number of dental offices that operate in the neighborhood, city, state or nation. Demand is the number of patients seeking dental care. When more patients seek dental care, it creates an imbalance, and either supply fills the gap (by opening more dental offices) or prices rise to reduce demand.

In this economy, demand has clearly diminished. Consumer Confidence, a measure based on consumers' perceptions of current business and employment conditions in the United States, has historically averaged around 93.2. As of October 2012, Consumer Confidence stands at 72.2. Consumer's willingness to spring for a latte is different from their propensity to seek dental care, but there is some correlation. Patients who have lost insurance (or jobs) aren't as willing to step into additional procedures, and self insured patients without employment can forgo or delay care. But, this is still Atlanta, and while demand has slipped a little bit, diminished demand doesn't tell the entire story.

What may look like diminished demand can be over supply. Last month we talked about dentists, in their late 50's and up, who had planned on retiring or selling out their practices in the next 5-10 years. Some dentists had planned to sell their practice this year, or last year or the year before. Unless those dentists exhibited extreme discipline in estate planning by reducing their holdings to only the safest investments as they neared retirement, they're probably holding on to their practices for another five to ten years to try and replace some of what was lost and to delay drawing down retirement funds. That hasn't stopped the number of young dentists who coming out of school, or just finishing up their 3, 5 or 7 year plan and are ready to open a new office. We're working with a number of dentists that wanted to purchase a practice, but because they find one, they are choosing to open a new location. New supply in these markets means there is less demand/patients to go around. This is a risk over which each of us have extremely limited control.

A second risk, that may look like a benefit now, is interest rate fluctuations. Solid producers in this market have numerous options to refinance right now. There are even options for offices that don't have strong financials, too. Some, out of necessity to bring down costs, and others out of greed to try and squeeze down one more percentage point, are choosing variable rates on long term obligations. We're not talking about the opportunities this month, but I'll leave this point saying that we have never been in a lower interest rate environment than we are now. That doesn't appear to be changing as we move into 2014, but what about 2017? Or 2020? The world economy being the only economy we have, there will be a time when things will stabilize and then accelerate and then get white hot again. I don't know when—no one does—but when it does, those who chose an extra 100 basis points for variable rate debts, or escalation tied to CPI, or short term mortgages stand to be huge losses. Like our current discourse involving the head of the CIA, it is incredible that some will risk so much in exchange for so little.

Third, are lease costs. Some of you have no control over this, but others of you have hit this risk right in the band. Behind staff salary costs, your rent should be your second highest cost. Every 3, 5, 7 or 10 years dental offices have the opportunity to reset their cost basis in this big category. This is almost not worth talking about because there is not much that can be done about it, but for those who have opportunities to negotiate or renegotiate their leases during this downturn, there is a great opportunity. We'll talk about the opportunity next month, but for now, it's important to understand the risk. Those who renew their lease casually or without professional help risk putting themselves at a much increased cost basis compared to others in the market. When your office is competing in a market with another office that has $1,000 or $2,000 or $3,000 less monthly cost than you do, then they have access to resources, marketing and incentives that your office may not have.

We've seen it time and time again—if my business is 15% better than my competitor's business, I don't pick up 15% more business—I pick up exponentially more business. This rule of exponential growth works in the inverse, too. If one business is 15% less than a direct competitor, then consumers will regularly choose the competitor. As the competitor picks up more patients, they add additional services and their business becomes 16, 17, 18% better. As the one business looses market share, they reduce services and the slide continues. Given a clear choice, 100% of consumers will choose the competitor whose business provides greater service.

The key word here is "clear choice." Consumers are not always able to discern which business is better, but we feel strongly that managing costs (or in the case of acquisitions—cost basis) is the best way to stay nimble in service lines.

The fourth risk in this market is the risks to retirement for all age groups. With market instability and supply and demand in flux, this is going to be one of the clearest dangers to dentist and their practices going forward. While failure to save for retirement may not sink us, it could drive many ashore.

America was built on the principal over the last 80 years that we're going to do, live and be better than our parents. In the 1950's, America had a strong middle class and it was bad form for a CEO to live large. Something broke for Americans in the 1980s and greed became good. Single working mothers that struggled to put food on the table bought expensive shoes for their kids. As for men, we all got caught up in luxury. What was bad form for those at the top of the food chain in the 1950's became a lifestyle that every American tries to project today. A vacation that a family would look forward to all year at the middle of the last century, has turned into a string of weekend and weeklong trips to Ritz Carlton's or other hotels around the area. Families struggle to afford a new house, new cars, nice clothes. We're richer than we've ever been and we simply can't afford it.

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This sounds cranky, but we have now entered into a time when college graduates are as interested in lifestyle as they are anything else. At a meeting with some of the city's best consultants, Larry Guzzardo said that our young workforce is more confident than they have ever been, but they're also less competent. This confidence has pushed them to complete tasks without any regard for protocol.

So how does this reflect retirement? The state of our young workforce is a reflection of the parents that raised them. We have a complete break in reality among Americans as to how we should live today and how much it takes to live like that. From our country to the family budget, no one is putting away enough money for retirement. Some will certainly drown, but even those that are able to stay solvent, the prospect of working to 70, 80 or beyond may literally run them ashore.

To sum it up, we have been through more economic uncertainty than other generations have seen. We looked at the following risks in our market:

1. Oversupply in the markets due to fewer practice transitions
2. Lease costs not allowing you to reduce costs to your patients
3. The risk of getting left behind on interest rate fluctuations
4. An inability to dial back lifestyle to provide for retirement

This has been a nice, uplifting look at the state of dentistry today, right? Well, there is a bright side. In our final installment, we're going to look at the opportunities and ways that dentists can take advantage of some unique parts of this market in 2014.

If you have questions or comments about any of the above, don't hesitate to reach out to me. We're helping dentists with these issues daily and would love to talk with you about how we can fit into your practice's real estate plans—or just grab a cup of coffee to talk about some of these larger issues.

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