

CAYDEN COLE: BACKHOE BUSINESS DECISION

Ron Mulholland wrote this case solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation. The author may have disguised certain names and other identifying information to protect confidentiality.

This publication may not be transmitted, photocopied, digitized, or otherwise reproduced in any form or by any means without the permission of the copyright holder. Reproduction of this material is not covered under authorization by any reproduction rights organization. To order copies or request permission to reproduce materials, contact Ivey Publishing, Ivey Business School, Western University, London, Ontario, Canada, N6G 0N1; (t) 519.661.3208; (e) cases@ivey.ca; www.iveycases.com.

Copyright © 2018, Ivey Business School Foundation

Version: 2018-10-05

In December 2014, Cayden Cole was sitting in the cab of his Hitachi ZX670 excavator, a 72,000-kilogram machine that could excavate a 14-metre radius and lift 10,000 kilograms per bucket load. He was working with Carmen Construction on a job at the Vale Sudbury Nickel Smelter Complex that involved expanding drainage ditches; but he needed to wait for the blasting contractor to finish drilling so he could place containment mats on the next section to be detonated. Cole did not like the monotony of waiting for an hour or two and then working briefly for 30 minutes before waiting again. As his thoughts drifted off, he considered the idea of buying his own backhoe and being his own boss.

HISTORY

Cole had completed high school, but he had to admit that high school was not the most enjoyable experience of his teenage years. What he really liked doing was driving and fixing any mobile equipment, whether it was the remote-controlled basketball shooting robot he helped build with his high-school robotics team or his dad's various trucks, loader, and backhoe. Of course, anything to do with snowmobiles, boats, personal watercraft, and cars was high on his list of activities and pursuits.

He had acquired this interest in driving and fixing machines from his father and grandfather—his dad was a Class A Mechanic with many other skills, and his grandfather was a welder, machinist, finishing carpenter, and jack-of-all-trades. Cole had spent many hours in the family garage taking apart various engines, electric appliances, and other operating machinery. He had a good idea of how things worked, how to fix them, and how to operate equipment and vehicles.

After graduating from high school in 2013, he got a job as a labourer with a construction company. The owner could see he was a hard worker, punctual, and eager to learn, and also that he was keen to be an equipment operator, as indicated by his willingness to stay late, wash machinery and vehicles, and move them around the yard. Cole's desire to be an operator was soon fulfilled, as he was assigned to a small loader for the upcoming snow removal season. He enjoyed this work, especially being in a heated cab, while the other labourers cleared walks and stairwells by hand-shovelling during the cold winter nights.

After the winter season, Cole decided to investigate other possibilities for heavy equipment operating. He was interested in moving on to a bigger machine. He placed an ad on Kijiji¹ offering his services as an “experienced” operator and waited to see what happened. He received two calls from potential employers—a construction company in Sudbury, Ontario and a road maintenance contractor on Manitoulin Island, Ontario, 1.5 hours away. He decided he liked the Manitoulin potential, so he set his truck up with a camper for accommodation and moved to the job. The owner let him park in the storage lot and plug in to the garage building. The camper became his new home away from home.

Cole worked there for five months but then winter was coming. He did not like the idea of sleeping in the camper when temperatures went down to -30°C , and he was not entirely satisfied with his treatment by the owner, so he again explored his options.

The first step was to call the construction company that had responded to his first Kijiji ad. Coincidentally, that company was looking for an operator again, so Cole jumped at the opportunity and was working for the company the next day. That was five months earlier, and although his supervisor had complimented him on the speed and tidiness of his work, Cole was already thinking about alternatives. One idea he had was purchasing a backhoe to become a contract operator.

BACKHOE OPERATION MARKET POTENTIAL

Cole had no idea how to attach a size to the backhoe market or how much business he could get. He wondered how many backhoes existed in the region and estimated there must be at least 100 in the area when he considered where he used to work; also, his dad and his cousin each had one. Typically 10 backhoes were posted for sale on Kijiji at any time. A glance at the Yellow Pages for Sudbury revealed 54 excavating contractors. Assuming at least one backhoe for every company listed in the Yellow Pages, and likely for each of those there was another one that was not advertised, he estimated there were 110 backhoe operators. He wanted to be number 111.

He decided not to worry about the demand side of the equation, but rather to concentrate on building up his own business by having a good reputation for operating safely, efficiently, and with a positive attitude. He estimated that in his first year he should be able to get 10 hours a week of paid work at CA\$70–\$80² per hour. In his second year, he thought he could get 20 hours per week, and by the third year, he hoped to be working, on average, 40 hours per week. For four months of winter—mid-December to mid-April—he estimated he would work only half-time due to lack of construction and heavy competition for snowplowing jobs.

INDEPENDENT BACKHOE OPERATOR BUSINESS INVESTIGATION

Cole had been watching constantly to see what machines and vehicles were for sale in the region. He stumbled upon an advertisement for a Case 580 backhoe that seemed like a good deal (see Exhibit 1). The machine had 3,600 hours (7,000 hours was typically considered the end of life for a backhoe), and the owner, who wanted to retire from the business, was asking \$43,000. The owner told Cole that he could get work with a local paving company, removing curbs, excavating roads, and doing other minor jobs. The owner had been doing that work with the machine before deciding to retire. He indicated there was much work available.

¹ Kijiji was the local online classified advertisement website.

² All currency amounts are in Canadian dollars.

Cole began to think about the costs for the business. He talked over the business with his father, and he looked on the web and found a site with information.³ Using the costs listed on this website, he came up with the following expenses for operating a backhoe. The operator should make \$20–\$30 per hour plus 20 per cent benefits. Fuel was the next big cost, requiring about eight litres per hour of operation. One day of work was typically from 7 a.m. to 5 p.m. and fuel was approximately \$1.20 per litre. Tires were another expense and amounted to \$3,600 per year for a set for an average 900-hour work year. Preventive maintenance included several activities related to oil, filters, and grease. This maintenance would cost about \$240 for each 500 hours of operation. Hydraulic hoses needed replacing and cost about \$500 per year. Rear bucket teeth and front bucket cutting edge maintenance was about \$80 and \$350 per year, respectively. Fuel filters would run about \$200, grease about \$50, hydraulic oil changes (per 2,000 hours) about \$200, and window replacement about \$2,000 per season. A busy year would be 2,000 hours.

FINANCING

Cole went to the bank to ask about a loan. He had about \$20,000 in an education fund that he was permitted to use. Purchasing the machine and having some money to operate for three months would cost Cole about \$50,000, so he would need a loan for \$30,000. The banker said he would not qualify because his credit score was too low. He needed some payment experience, so the banker suggested that Cole put the \$20,000 in the bank and deposit \$600 a month for six months. He would then be approved for a loan with a five-year amortization, and a 6 per cent interest rate.

Not wanting to wait, Cole went to a local equipment leasing company, Money in Motion, and filled out an application. This company seemed likely to lend him the money based on his down payment and the value of the machine. The only catch was the 12 per cent interest rate! This company also mentioned he should consider getting bookkeeping help at \$1,500 for the year and insurance that would be approximately \$2,200 for the year. Cole had also heard that it was better to incorporate bookkeeping because insurance and taxes would be less.

DECISION TIME

Cole had some serious thinking to do. He was making \$22 an hour on the job and working 50 hours each week. Although it was boring at times, it was a regular wage. He was a bit worried about how much work he might be able to get. In the winter months, December to March, he speculated he could work clearing snow; in the spring, summer, and fall, he hoped to work with the same paving contractor the previous owner had. That job paid \$85 per hour, and although he had heard some companies paid higher rates (up to \$105 per hour), he was concerned about the number of billable hours he would accumulate. He had previously thought he could work the machine 40 hours per week for 48 weeks, but he had read and heard from others that 900–1,000 hours was more likely the average number of hours per year. He hoped he could do half that in his first year. He wondered about getting some help from his uncle, a business professor, on making the decision. As he was contemplating this situation, the site supervisor indicated it was time to move some more blasting mats. Cole vowed to himself that he would investigate and make the decision to buy or not buy the backhoe and become an independent contractor within the next four weeks. Then, he fired up his machine and got back to work.

³ "O & O Costs: Backhoes," Equipment World, May 3, 2008, accessed January 6, 2015, www.equipmentworld.com/oo-costs-backhoes/.

EXHIBIT 1: A POTENTIAL BACKHOE FOR SALE



SM Series 2, four-wheel drive, extendahoe, pilot controls,
pattern switch, rear auxiliary hydraulics, 3,600 hours total time.

Price: \$43,000

Location: Hanmer, Ontario P3P 1Y7

Call 705-207-####

Source: Case author.