

27th Weekly Crisis-era Message to Contractors from: Dr Tom Schleifer
Reader Questions and Answers

Reader's Question: Dr Schleifer, Three of our major projects were delayed in April. Two continue to be indefinitely delayed and the third has canceled. We managed to grab two smaller projects, but our aggressive pricing is already backfiring on us. Sales for the year will be down at least 25% and while a few projects are doing all right, we have consumed our profits from January through mid-March and without a miracle we will have a loss for the year. We have cut all non-essential costs and furloughed a clerical person. Some of our construction people have been with us 20-plus years and I can't afford to lose any of them. Any suggestions?

I wish I had the option to avoid this question and, while it will be no consolation, you are not alone. There are others, worded differently, but the same problem. This crisis will impact most construction enterprises but some more than others depending on type of work and the level of competition in their market. For the same reason, a small number may not be impacted at all or to a minor extent. You have an advantage in recognizing this early because others with the same exposures are moving forward based on hope more than logic.

It sounds like you already know that chasing more work to fix the volume reduction is not a viable option. Again, you are not alone. Available projects from here on out will be subject to aggressive competition, aggressive pricing and offer limited profit at best so attempting to maintain sales (top line) magnifies the risk and will not work. It is akin to using gasoline to put out a fire. I use the expression: "more cheap work is just more cheap work". I understand that you are convinced that you cannot afford to lose any of your key people. That said, I can assure you that unless you have serious cash reserves that you are willing to spend, losing money this early in the crisis exposes your firm to running out of cash before the recovery or not having the ability to finance your firm's growth when more work becomes available.

I spent more than ten years researching solutions to the problem and discovered only one. No business can or should lose money if there is an alternative. You have 75% of the work you planned on and that work has potential profit within it. It might be modest profit but it is profit and, at some point in your firm's history, the dollar value of that 75% was your total sales. I venture to guess that you made a profit executing that amount of work in the past. To profit from that amount of work now you have to reduce your cost of doing business to roughly what it was then. You can take the percent of sales your overhead was last year and reduce your current overhead to that percent of the amount of work you have on hand. Overhead has to be adjusted.

May I take this opportunity to apologize in advance if this sounds insensitive. I have been in my own business my entire career and always agonized over having to lay off employees, even if it was for cause. I know how it feels.

I can't tell you where or who to cut because you alone are intimate with how your organization functions. You also know that a construction company's overhead is 90% or more employees. The other overhead costs always have some waste in them that should be cut, but not enough to matter. What I can tell you is that reduction is critical and the most effective approach is to cut more rather than less because you are dealing with the survival of the company and the continuing employment of the 75% of the employees who remain. For example, if you have 10 employees in question and need to cut 25% which is 2.5 people that means three people not two. There are several reasons. Things often get worse

before they get better. The extra 50% of the cost of this one employee of ten is 5% of the total and way more than can be risked under these circumstances. If two are laid off and later another, it creates a serious morale issue with the remaining seven. Cutting more rather than less is a prudent safety precaution and far less emotional stress on all concerned to do it once rather than twice.

There is and always will be the argument that the work on hand needs to be completed. I am widely published saying “the production of the work according to plans, specifications and schedule is critically important and that includes schedule”. In these circumstances the customer is the primary concern, but if the company does not survive, the project will not be finished by the current contractor. To assure performance, the cutbacks need to be made in advance and progress will be affected--projects may be delivered late. I have heard before: “There must be an alternative”. If anyone finds one, please send it in. Always cut more than less. Like all business decisions the prudent safest course of action that minimizes risk is always better than what is expedient. No professional has the luxury of choosing what is emotionally easier.

The selection process of who gets laid off was raised in another question and that answer applies here as well. Reader’s Question: *Tom, What’s the first step in cutting overhead? Is it last in/first out or is it a functional redesign? What do you recommend?*

There are obvious financial advantages to cutting overhead sooner rather than later, and there are some practical issues that operate in favor of the production of the work. Who gets laid off is a decision that senior management is stuck with. Last in/first out to some people is considered “fair” and others consider it arbitrary and unnecessary. This is clearly management’s choice. Absent any contract or legal requirements, under these circumstances what is best for the organization would be based on merit. My experience is that the best employees remain based on skills and value. This leaves a highly motivated and skilled team that have, in many past cases, exceeded expectations and set records for execution, profitability, and schedule. This is perhaps the best result in a bad situation.

Losing highly trained and skilled people that the firm has an investment in cannot be avoided, however, the replacement of these positions may not be as difficult as imagined. A market recovery takes time and at the end of the downturn there are many unemployed to choose from. When I addressed this point at a seminar during the 2009-2012 recession the regional CEO for a national firm raised his hand and said: “As I think about what you are saying, there are a few managers I would not miss too much, and now I am thinking that if I lay them off I may actually have the opportunity to upgrade some of these positions when I replace them during the recovery”. I think that best sums up what I was trying to say on the topic.

Next week: Reader’s Questions and Comments. [Send questions/comments to tom@schleifer.com](mailto:tom@schleifer.com).

To receive the free weekly Crisis Message send your email address to tom@schleifer.com.

Note: Overhead management information is found on letstalkbusiness.net click on “Manual”, then Managing Overhead in the table of contents.

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