

Avoiding Losing Projects (Back to [Table of Contents](#))

The construction business growth model that most of us grew up with is not working and is totally inappropriate in a cyclical industry. When I was learning the business I was often told “If you’re not growing, you are going backwards”. Most of the construction enterprises I am familiar with embrace or are strongly influenced by a business model driven by growth which puts much too much pressure on increasing sales; or at the least, to maintain volume for the sole purpose of covering overhead.

Industry Beliefs

There are well-established construction industry beliefs that need to be reconsidered. For example: *Growth is always good, Overhead is a symbol of success and not to be surrendered unless absolutely forced to; Cutting overhead is an admission of failure; Down times are bad news but a natural part of the industry; The industry is not necessarily cyclical; Unprofitable work is just part of the business.* These beliefs cause many to go after whatever projects are available in good times or bad whether or not their organization has experience with the work, the owner, the designer, the size of job or the geographic area. A lack of experience with any of these dramatically increases risk, but most of us refuse to give up hard-earned growth. Taking on work we have limited experience with can result in what I call the “80/20 problem”.

80/20 Problem

From a study of hundreds of failed construction companies I determined that all of the financially distressed firms had an abundance of profitable work. Their problem was too much unprofitable work. It is fair to say that many, if not most, construction enterprises have occasional losing projects. As mentioned above, it is a well-established industry belief that “some unprofitable work is just part of the business”. The companies that failed had on average 80% profitable work and 20% unprofitable work. The number of unprofitable jobs or size of the losses simply grew beyond what the profitable work could support. While the profit reduction was a major issue, overhead was often the larger problem. Let’s look at an example:

Case Study

A contractor with \$10 million annual sales has \$1 million overhead (Not recommending 10% overhead—just easy math). Eighty percent of the work, or \$8 million, is generating 13% profit or \$1,040,000 of which \$800,000 is the contribution to the 10% overhead and \$240,000 is net profit. However 20% of the work, or \$2 million, is generating a loss of -5% or -\$100,000. This loss is offset against the \$240,000 net profit earned by the 80% profitable work netting \$140,000. However, the \$2 million of unprofitable work contributed nothing toward the 10%, or \$200,000, overhead anticipated to be earned from that work which now must be funded by the profitable work of which there is only \$140,000 remaining which. This results in a -\$60,000 loss for the year. If unprofitable work is just part of the business, (and I am not convinced of that) then at the very least, minimizing the amount of unprofitable work must be a priority focus of management.

No Bad Projects

I spent years studying, defining and measuring the causes of business failures which led me into research on how to reverse or manage losing or failing projects while they are in progress. I confirmed that it is incredibly difficult to reverse troubled projects, hugely expensive to manage

them, difficult to eliminate the damage once done and impossible to minimize costs already incurred. What I did discover was that the primary cause of project failures is inexperience with the type of work, project, or process. I also discovered that gaining necessary experience is the problem—not the solution. Fast forward to the results: The only solution determined was PREVENTION—not taking the losing project. The research confirmed something else that I agonized over for years and refused to state in public until I confirmed it conclusively: There Are No Bad Projects--Just Bad Matches of Contractors to Projects. Project Failures don't just happen; they are jobs that are deliberately pursued and captured.

Project Experience

Experience is a “Paradox of Industrial Proportion” because it is fair to ask: “If experience is critical to success, how do I gain the initial experience?” This leads to another question: “Should a construction enterprise ever take on work they have never performed before?” This issue is a matter of risk tolerance and a decision about emphasizing profit or volume. It is clearly a contractor's choice to make. However decision-makers should understand that they buy experience. Knowledge and experience are purchased, never free, can be extremely expensive and there are serious risks associated with the process. A good thing to keep in mind would be to expect the unexpected. When work is attempted that an organization has limited experience with there are some guidelines that may help: Start small; Finish the first project completely before attempting another and Attempt only what you can afford to lose.

Measuring Pre Project Risk

When I set out to research pre project risk I discovered that there are three critical elements: Experience, Experience and Experience. I determined that quantifying pre-project risks is directly, and possibly exclusively, correlated with an organization's experience with similar work. Therefore pre project risk in a project is completely different for every contractor. The most important discovery was that pre project risk CAN BE MEASURED. Construction risks are unique; and unlike manufacturing, where improvements result from repetition, construction projects have limited repetition or duplication because most projects differ in significant ways. Limited replication confines experience to similar prior projects that have been priced, built and collected for at a profit. Therefore, direct experience with the size, location, type and design of the work is critical to success. The more similar a new project is to previous successful projects, the more likely estimated performance will be achieved. The reason of course is that planning and execution is more of the same as opposed to totally unique. Experience is accumulated institutionally, but captured individually, consequently the number of team members with direct experience on similar projects is important and can dramatically impact the likelihood of achieving estimated or improved project performance.

Project Selection program:

The research confirmed the need for a process to screen out losing projects at the pre project stage to enhance overall profitability? The development of the program took another year and a half and resulted in an easy-to-use tool that can also be used as a check list. The **Project Selection Program** has been put into the public domain and can be downloaded free at: www.SimplarInstitute.com/ProjectSelectionProgram. During beta testing numerous contractors ran the program on three completed projects—two successful projects and one project they wish they had not taken. They answered the 26 individually weighed questions