

29th Weekly Crisis-era Message to Contractors from: Dr Tom Schleifer
Reader Questions and Answers

Reader's Question: Dr Schleifer, My trade association and my lawyer say that I will be paid for the cost of the new COVID protocols I am forced to put in place. From what you said in your message last week, it sounds like you are saying we will not be reimbursed for these costs. Why do you think that and what do you suggest we do about it?

Answer: You are not alone in challenging my answer to the question last week about the costs of complying with the required COVID jobsite protocols. There were a lot of challenges and some not as courteous as yours. Just to clarify, I did not say *"we will not be reimbursed for these costs"*. What I did say, based solely on past experience, was: *"Whether contractors will be compensated for them (COVID costs) is a legal question and I am not an attorney. I do have some concerns"*. I went on to explain that after exposure to thousands of construction claims they don't always turn out as expected. I suggested that *"collecting for these unforeseen costs is not a sure thing, that results will vary from project to project, and when you will collect is also an issue"*.

I stand by these comments because I consider a risk like not being compensated in full, no matter how small you believe it is, to be too serious to discount. I firmly believe that the only prudent course of action under these circumstances is as I stated last week: *"I suggest that you strictly adhere to the letter of, and intent of, the COVID job-site protocols and requirements and that you make every effort to minimize the costs of these requirements as you would any other project activity. I recommend that you manage and plan the financial aspects of your business assuming you will not be compensated for these costs and assume that if you are compensated you may collect long after you have a critical need for the cashflow. Scrupulously manage all costs on all projects and consider reducing the cost of doing business because cashflow will likely be tight unless or until you have strong indication that you will be compensated in a timely manner."*

I clearly said "might" not be compensated in full, which I stand by, and the ultimate test for anyone who says you "will" collect would be to ask if there are any odds associated with the issue. Unless it is 100% certain, it is "might". Some may be satisfied with 99%, but I am not sure that is prudent when you are betting your business on it because, for some firms, the costs are enough to cause losses. My concern stems from the reality that few people have been exposed to as many construction claims as I have. Over more than a decade my surety consulting firm dealt with thousands of financially distressed companies nation-wide for sureties and, as you might imagine, these businesses had numerous claims of every description. We had to report on the circumstances and often participate in the resolutions. Our experience was that there was no sure thing, which is probably why we call them "claims". I realize that much of this is a restatement and sincerely hope that this is responsive to your question. Please feel free to contact me directly if you feel the need to discuss further.

Reader's Question: Tom, You say this is a market cycle and that the construction market has always been cyclical, so if this is just another cycle won't we just get through it like we always have?

Answer: Market cycle means a period of market decline followed by growth, or a period of market growth followed by a decline which this current circumstance obviously is. The reason it is referred to as a cycle is that it happens periodically and, in the case of the construction market, regularly (about every 10 years). The cause of construction market cycles is an alteration the US economy (or adjustment, as economists refer to it), which is the cause of this construction market cycle. The fact that the US economic downturn was caused by a unique event, the COVID-19 pandemic, does not change the

definition of this as a construction market cycle, nor does the unique event change the predictable impacts on the construction industry, other than the cost of the on-site COVID protocols required.

The recovery of the construction market is dependent on the recovery of the US economy, therefore, in order to project the recovery of the construction market we need to study the cause of the US economic downturn. For each cycle there are underlying causes like the recession that started in 2008, which is often referred to as the US subprime mortgage crisis. This is the eighth major construction market cycle since World War II and research on the prior seven cycles has provided a model of how the construction market reacts to changes in the economy during both the decline and the recovery stages. With the new model we are now able to accurately project how the construction market will react and when.

Specific to your question, “won’t we just get through it [this cycle] like we always have?” The answer is, “YES we will” which is exactly what I was hoping to prevent with these Crisis-era Messages to Contractors which began in March. The results of how we got through the prior cycles were not pretty. The cycles caused our industry to suffer severe reductions in profit along with serious financial distress and an unfortunate number of construction business failures. When it became obvious that the construction market was entering another downturn cycle, this message series was intended as a warning that we needed to react quickly to avoid going through what we always have. Our industry reacts poorly to a declining market with most contractors unwilling to downsize without a fight. The “fight” is aggressive pricing in an attempt to capture as much as possible of the lesser amount of work available. This drives profit margins down and leads to some inappropriate decisions.

Change of Schedule: This is an appropriate juncture to reduce the frequency and coverage of these message because I find myself repeating solutions. The solutions are distasteful within our industry and data about the length of the recovery is unpopular so there is less to write about. This is apparent by the number of associations that understand the content but are unwilling to circulate the messages saying, “*they are just too negative for our members*”. In an effort to keep in touch with those who have a continuing interest or questions, the messages will be reduced to twice a month for a while. The next will be in mid-October. In the meantime, keep the questions coming and feel free to contact me directly if you need to talk.

Send questions/comments to 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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