

Third Crisis-era Message to Contractors from: Dr Tom Schleifer

Why a Measured Response and When?

We are all in this together and doing our part to stem the spread of the virus. Most fear that this is not a pause but a tsunami. Which it is, in that the effects will be felt well beyond health issues, and for a long time after they are under control. It is difficult to plan a business response when we are contemplating what it will take to solve the bigger problem affecting the entire human race. In fact, most contractors are convinced that they have to wait and see where all this is going before they can even consider the impact on their business. My concern is that time is not on our side and that when we finally realize how this will unfold, we may discover that the solution for our company is long overdue. As with so much in life, timing can be critical

When we develop business plans in “normal” times we project into the future which, of course, is unknown, but we have no choice. We plan to our “planning horizon” which includes our belief in what the future holds and our level of confidence in that belief (the odds). We use what we know, search for additional information and strategize accordingly. In the current circumstances there are plenty of unknowns, but also enough data trends to project far enough into the future with reasonable accuracy to formulate what to do now with considerable confidence. This is not the time for emotional or knee-jerk reactions. We all want to be good citizens and good people and most feel responsible to employ as many people as possible during this crisis and I applaud those feelings. What I am recommending is that you make certain in advance that your company can afford to do that and for how long.

We can expect some relief from restrictions when there is evidence that the incidence curve is heading down and with any luck the stock market should respond favorably. The question for us is: When will the construction market rebound from delayed and canceled projects, and will new capital spending be available to fund new projects? This will depend on the US economy rebounding which can't happen overnight. The first project cancellations were in mid-March, which for our purposes can be considered the beginning of the crisis impact on our industry. We can define a total rebound as when the annual rate of construction put in place meets or exceeds the rate it was before this started.

As an exercise let's explore when you, the reader, think total rebound might occur. I will express possibilities while you adjust your calculations to your own beliefs. Most restrictions have already been extended through April. When the virus incidence cure rate starts heading down, restrictions will be reduced. Take your best guess when that will happen. Let's be optimistic and say mid-May. However even after that

milestone, there will still be tens of thousands of people sick, others testing positive, and virus concerns will still be in the news; so everyone will not be racing back to work. Some work will resume, but total economic recovery is unlikely. Based on length of continuing illness and even with a reduced rate of virus spread, it is probably safe to say that total construction rebound will not happen for quite a few months after the incidence curve starts down. After that it will take some time for remobilization, so my guess is that the most optimistic possibility for full production is out six months at a minimum.

In the meantime, public entities will have suffered extreme reductions in tax revenues, and private industry will have experienced severe losses from lack of activity which will undoubtedly result in conservation of cash, impacting the restart of delayed projects and potentially more cancellations.

Absent full recovery, the deficiency will obviously be shared unevenly among construction enterprises based on backlog, cancellations, delays, etc. The prudent contractor should decide now for themselves if they can afford their full overhead if their sales fall off for four, six, eight months or more. The worst case is trying to absorb it for months and then finding it will last longer.

Note: Additional information on how to cut overhead can be found on letstalkbusiness.net. Click on "Manual" and go to Managing Overhead in the table of contents.

Next week: How the shock to the US economy will impact the construction industry long-term. To assure you will continue to receive the free weekly Crisis Message to Contractors, you will need to send your email address to tom@schleifer.com.