

# Growing out of business, Part IV



Submitted by  
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## When is the time right to cut margins?

Construction companies work in a difficult and competitive environment. For both general and subcontractors, there is a constant influx of new competitors. Many of these new players do not know how to appropriately price their work, and as a result, most of them will be gone in just a few years.

Construction professionals like to joke that they compete with "everyone who has a pickup truck." Like most commonly heard jokes, there is a lot of truth in that statement. With the boom in residential, commercial and industrial construction projects around South Texas over the past few years, more "pickup truck contractors" have entered the business than ever before.

Yet it is not just new competitors that make the bidding market difficult. Current issues in the financial markets, along with inflation in the cost of commodities and materials, are squeezing margins for all businessmen, and especially for construction companies. The local decline in residential construction is pushing increasing numbers of competitors into those sectors that are still thriving.

When the building cycle gets highly competitive, it is not unusual to see jobs awarded to bidders who seem to be pricing below the cost of production. It can be frustrating to any well-run organization. Knowing that you are trimming your bid as closely as you can while remaining financially viable doesn't help if you have no work.

How can you determine when it is appropriate to cut profit margins to a break-even level? Many contractors will do this to "fill the pipeline" rather than face a lay-off of loyal personnel. Others do it because they need to maintain cash flow.

While there may be legitimate reasons to take a profitless job as a temporary strategy, it should only be considered if you can answer each of the following questions with "yes."

Have you reviewed any increases in structural expenses over the last 12 months? In good times, we tend to add services, subscriptions and repetitive items to our overhead that were not previously necessary. If you are having trouble landing jobs profitably, it's time to roll

back those luxuries.

Have you reviewed every new hire you made in the last 12 months? Like overhead expenses, people are added when we are busy. A good employee will always look for work to keep them occupied all day. That does not mean their job is as necessary as it was when times were better.

Are you sure that the current market is temporary? Unless you can clearly see an upsurge of work on the horizon, restructuring your company now may be an inevitable requirement for long-term survival.

Is this a "one-time-only" occurrence? No company can abandon profitability for any length of time and survive. Bidding one job low to bridge a short-term problem is far different than electing involuntary and ongoing not-for-profit status.

Do you have a financial fallback position? Pricing a job close to the vest leaves less margin for error. Make sure you have the cash reserves or credit facilities to withstand a mistake.

Just as new competitors are like mushrooms after a rainstorm in an expanding market, many will shrivel up and blow away when the market contracts.

Every business may have to face reduced margins in more difficult times. If you face that problem, make sure that you have identified the actions that will allow you to emerge successfully from the other side.

*Coming next month: Focus is the key to success.*

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