The Six Big Profit Killers

by Philip Thaut

The Rutlidge Institute is the pricing research and software company that spent nearly three years developing the *National Renovation & Insurance Repair Estimato* for Craftsman Book Company. Research for the price book focused not only on costs, but also on other conditions that make the difference between making money and losing money. Analysis of construction companies from all over the country led to the following list of the top six profit killers.

Profit Killer #1: Waste

The cycle begins with overbuying of materials. Rather than come up one board or one brick short, many construction managers overbuy by several units. While this saves a time-consuming trip to the supply house, it creates a large quantity of leftover materials.

This leads to the second step in the cycle — inefficient storage. Most construction company warehouses are disorganized, and many stored materials are ruined when they are allowed to freeze or overheat or when new materials are stacked on top.

Even well-kept storage facilities are seldom used as intended. Except for nails, workers rarely consider looking for materials in the warehouse, choosing instead to buy new materials for each job. This behavior also applies to small hand tools, like nail punches or chisels. Many workers lose these tools over and over again and buy new ones at the company's expense.

Unskilled help A second source of waste stems from unskilled workers, who ruin far more materials than do skilled workers. Rutlidge encountered many examples of this, including special-order beams that were cut too short, whole series of rafters cut to an incorrect pattern, and so on. Many companies are more endangered by success than by slow times because of the incredible waste generated by unskilled workers, who are hired in a hurry and not properly trained.

Solutions:

- Move materials directly from one site to the next.
- Keep track of inventory, and arrange to have materials delivered.
- Estimate materials accurately.
- Use a "buddy system," pairing skilled and unskilled workers.

Profit Killer #2: Inefficiency

Many renovation and repair jobs are poorly scheduled. Painters arrive before the drywall is finished; insulation is installed before the electrician is finished; workers show up without proper tools or materials, or they are pulled off one job to handle another. It is also common to find that the most skilled worker on site spends the majority of his or her time running errands that any unskilled laborer could do.

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In one case, Rutlidge concluded that the difference between a profitable company and a nearly identical company facing failure was a secretary who made little more than minimum wage. She organized the office and the crew heads so efficiently that she always knew the status of all jobs. When a foreman was in danger of allocating labor unwisely, she was able to advise differently based on the larger picture. The result was crews that ran efficiently and always had the materials and tools they needed.

Solutions:

- Match workers to the job.
- Send the least-skilled worker on errands with clear instructions on the tools or material to be retrieved.
- Hire a production manager or designate one person in the office as keeper of the schedule.

Profit Killer #3: Free Work

One of the biggest ironies in construction is that contractors who do work for free have more dissatisfied customers than contractors who don't. For example, one contractor Rutlidge observed was replacing windows in a fire-damaged home. All the windows on the front of the house were replaced except one. The new windows were much more energy efficient and attractive, so the contractor suggested that the owner replace the one remaining window.

When the owner declined, the contractor — who took pride in his work — replaced the window at his own expense. Later, he also upgraded the base molding in the home, and installed soffit and fascia on a section of roof where it didn't exist before — all at his own expense.

The result was an unhappy customer. The customer reasoned that if the contractor can afford to replace a window (something the owner felt he couldn't afford to do), then the contractor must be making a lot of money at the homeowner's expense. The homeowner began to push for more and more "free" work, and tension rose.

Nobody wins in this type of situation. The contractor doesn't understand why the customer doesn't appreciate all the extras already received. The homeowners feel they have signed a contract that gives the contractor too much, so they aggressively look for ways to recover what they think is an overpayment.

Solutions:

- Charge for every modification, no matter how small.
- Document every change with a signed change order.
- Charge for delays caused by changes.
- Never believe a homeowner who says, "I'll pay whatever it costs, just bill me."

Profit Killer #4: A Talkative or Picky Homeowner

Clients who worry over gaps in framing, holes drilled for plumbing, or shading in brick, and who want to talk about it — to you, your workers, your subcontractors, and everyone at your office — can steal all the profits from a job. So can homeowners who question every process and provide unneeded and sometimes disastrous help, and who want to see sample after sample before making a final decision.

Solutions:
- Evaluate every homeowner and, when necessary, raise the price of the estimate as much as 30% to cover the "headache factor."
- Build in penalties for failure to make timely decisions.
- If you can't raise prices, don't take the job. If you aren't going to be compensated for working with this type of homeowner, the best thing you can do for your business is to let this job go to your competitor.

Profit Killer #5: Communication Breakdown

The husband said, "Paint the room yellow"; the wife came in later and said, "No, paint it white." The husband told the painter; the wife told the contractor; the contractor told the painter's receptionist. When she told the painter, he said, "That's not right. I just talked to the husband," and painted the room yellow. The contractor blames the painter, the husband says it was really the wife's decision, and on and on.

Solutions:
- Establish a single decision maker — either the husband, wife, or someone else, but never more than one person.
- Do the same internally — one person from your company must be the contact.
- Train all workers and subs to politely but firmly decline to accept a decision or to make one.

Profit Killer #6: Underestimating Complexity

Even a novice estimator understands that increasing complexity will also increase labor and waste. But in practice, even the most skilled estimators fail to realize just how much complexity can add to costs.

For example, Rutlidge found a small remodeler who had estimated the cost to hang drywall in a finished attic with five dormers. Because the drywall would be hung on many small sloped ceilings, the drywaller added 50% to his normal price.

After the job was complete, Rutlidge determined that the drywaller should have charged over 300% more for this portion of the work. Because the contractor underestimated the effects of complexity, he earned less than minimum wage for his drywall work in the attic.

Underestimating complexity has become more common in recent years with the increased use of computer estimating software. These programs can make estimating quick and easy, but few provide any good way to allow for complexity. As a result, Rutlidge research has found, many estimators rely on the "built-in" costs from the supplied database 90% of the time. Rutlidge believes, however, that built-in costs only match the situation about 55% of the time.

Solutions:
- Use prices from cost books and computer databases only when the line items match job conditions exactly.
- Use historical job-cost data to adjust built-in prices to allow for complexity.

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