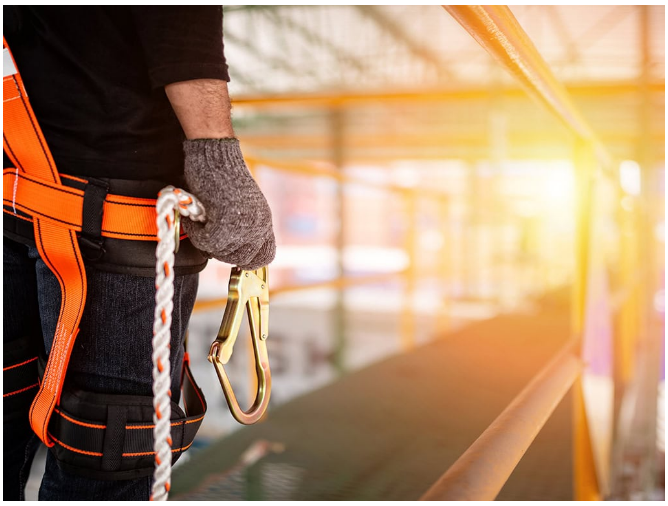
PROTECT YOUR PROFIT: 5 TIPS FOR PREVENTING PROFIT FADE



Profit fade, or the decline of expected gross profits over the course of a project, can be a serious problem for construction companies. Not only does it directly erode the bottom line, but it is also an indication to sureties and lenders that the contractor may not be able to effectively estimate and manage job costs.

There are many potential drivers of profit fade, including overly optimistic estimates, inaccurate job costs, unbillable change orders, unexpected job-site conditions and supply chain issues. Some causes of profit fade are ultimately out of the contractor's control (i.e. adverse weather conditions), but some drivers can be avoided.

Here are five proactive tips you can leverage to help avoid profit fade.

1. Budget for success

Contractors need a realistic budget based on the original bid to serve as a guidepost for the measurement of job performance and identification of profit fade. Job budgets should consider pre-construction costs, hard costs such as equipment, materials, and labor, overhead, and projected revenues. The larger the project, the more beneficial a granular, detailed budget by phase will be to protecting job profitability.

2. Monitor work in progress

To be effective, the budget needs to be top of mind and constantly monitored, not simply put on a shelf or filed away. As a job progresses, track and investigate any variances between budgeted and actual performance. Depending on the size and complexity of the organization, contractors can benefit from the real-time visibility that utilizing job-costing software to track costs and monitor change orders provides. Prepare regular work-in-progress reports to track:

- Contract prices
- Amounts billed and costs incurred to date
- Projected final costs
- Estimated gross profits

Continuously tracking this information alerts you to problems early and allows you to address them before it's too late.

3. Get a handle on job costs

Evaluate your estimating and job costing systems and processes to be sure they're accurate and complete. Ensure that the proper parties are routinely involved; for example, how can projected costs be monitored without the input of the project manager, who has boots on the ground?

4. Build protections into your contracts

It's hard to avoid profit fade if your contracts are vaguely worded or make it easy for the owner to change the project's scope. To minimize unanticipated costs, double-check that your contracts clearly define the nature and scope of work and set forth straightforward change-order procedures that ensure you're compensated for extra work.

5. Learn from your completed jobs

Routinely perform a gain/fade analysis, comparing gross project at contract completion to prior estimates, analyzing for patterns and trends. Determine whether profit fade is associated with certain types of jobs, locations, customers or personnel. If you identify a clear cause, address it immediately.

Unfortunately, in today's uncertain economy of rising costs, there's no way to eliminate the possibility of profit fade altogether. However, by identifying factors associated with this common problem, you can take steps to prevent it from adversely affecting your financial performance on future jobs.