



Document WP15

MARCH 2018

# The Top 10 Reasons Contractors **SUCCEED**

DENNIS ENGELBRECHT  
WAYNE RIVERS

## INTRODUCTION

Many of you are familiar with the articles and books written about why contractors fail – there are a host of them. While these pieces lay out the commonalities of distress and failure, they leave open the question of how to assure success. And while achieving success is partly the obverse of avoiding failure, they are hardly identical.

For the past 15 years, The Family Business Institute has been running peer programs for commercial contractors, and a number of clear, teachable lessons emerged from the most successful businesses. This paper will lay out the top ten ways the most successful commercial contractors have gone from good to great.

## DEFINING LONG TERM SUCCESS

Financial results have to be an important indicator in defining contractor success, of course. But financial success is often the result of many other business factors any one of which may represent success in non-financial terms. Depending upon how deeply one dives into detail, the list could be exhaustive. For the sake of brevity, let us propose the following definitions of success in construction:

1. **Sustainability:** The company is sustainable in good economic times and bad, from the current generation of leadership through the next
2. **Culture:** The organization is strong, positive, and safe
3. **Great People:** The company is populated by personnel who have talent, drive, virtue, and work well with each other and industry partners
4. **Lifestyle Balance:** Owners and employees balance work with family, personal health, and community with reasonable stress levels
5. **Performance:** The company's financial results exceed industry norms for margins, returns, and growth

Could a business declare itself successful based upon just items two, three, and four? Certainly! However, without financial performance and growth there won't be sustainability. And the firm might lack the opportunities and rewards necessary to attract and motivate the best and brightest. Can a company achieve financial performance without factors two and three? Not over the long term, and short-term success might come at a tremendous personal cost. Can a contractor attract great people without a strong and positive culture? Possibly. But, it can't happen consistently without either overpaying or having retention and turnover issues. One success factor inevitably supports and strengthens the others, and a balanced approach almost always beats a myopic focus on merely one or two.

Let's take a deeper look at the commonalities and characteristics that have helped create a very high level of success for a few good contractors and how you can implement proven success strategies to assure your own prosperity.

## The Top 10 Reasons Contractors Succeed

### 1. Successful Construction Companies Have Effective Leadership

When reviewing the more successful members of our peer group program, there are three main commonalities among the firms' leaders.

**Drive:** It is not necessarily a drive to be bigger - although that ambition is there in some cases. Mostly they display a drive to be better or more than they are currently – to take what they have (already quite successful) and to improve. In short, they aspire to excellence! That excellence is never narrow; it embraces people, quality, service, community, relationships, safety, and bottom line results. Self-improvement and self-awareness are key initiatives for great leaders who aspire to get even better.

**Servant Leadership:** Successful companies tend to be purpose driven. Individual leaders lack the ego and greed that might repel good people and prevent them from joining the cause. Only one of our 30 most successful construction companies is still steered by its founder. Most are now led by carefully selected next generation leaders who have been chosen from among the potential candidates for their leadership characteristics as opposed to their genetic connections. Merit, not nepotism, has been the successor selection criteria for the most successful firms.

In *Leadership is An Art* by Max DePree, he says the “first responsibility of a leader is to define reality. The last is to say thank you. In between the two, the leader must become a servant and a debtor. That sums up the progress of an artful leader.” He also writes that “the only kind of leadership worth following is based on vision...” and that “personal character must be uppermost...” If we were to summarize the book in a simple form the following table provides a contrast between fifteen common perceptions about leadership versus DePree’s definitions on the art of leadership.

Common Leadership Perceptions	Reality of True Leadership
Charismatic personality	Maybe; maybe not
Craves personal achievement	Enables others to achieve their fullest potentials
Tells other what to do	Liberates people to do what is needed in the most effective ways they can
Autocrat, controlling, micromanaging	Abandons self to the strengths of others
Tells	Listens
Science	Art
Knows it all; the EXPERT	Knows he/she can't know everything about anything
Inflicts pain	Bears pain
Has servants	Is a servant
Sets goals	Facilitates goal setting
Makes decisions	Participates in making decisions and facilitates others making them
Holds others accountable	Holds other accountable while simultaneously BEING ACCOUNTABLE
Owns (possesses) the business	Is a steward of the business
Tells others what they do wrong	Pats people on the back
Leaves behind a legend	Leaves lasting success

Leadership isn't about taking charge and dominating; it is about finding ways to make others around you more successful and employing a virtuous process for everyone's mutual gain.

**Focus on Executive Functions:** Successful companies have leaders who are involved and interconnected. None has an "ivory tower leader" who pulls the strings from afar and sits back counting money. Leaders know what is going on. They fight the daily battles with their people; however, they are not directly managing or estimating work. They have intentionally evolved beyond the daily tasks that others can do as well as they can, and this focus on strategic, big picture leadership has unleashed their companies to move forward to bigger and better things. For those that focus on managing people and relationships instead of tasks, the dividends are self-evident in that they not only have more successful enterprises, they enjoy healthier, better balanced lifestyles as well. One of our most successful contractors embraces "Humble, Hungry, and Smart" as a core guiding principal. That slogan fits most of our other successful leaders as well.

While discussing the subject of leadership, it is appropriate to also talk about the phenomenon of "followership". In 2013, Google took a deeper look into followership, and they determined that high-performing teams exhibited five characteristics.

1. Psychological safety: Team members feel safe to take risks and be vulnerable in front of each other
2. Dependability: Team members get things done on time and meet the organization standard for strong performance
3. Structure and Clarity: Team members have clear roles, plans, and goals
4. Meaning: Work is personally important to team members
5. Impact: Team members think their work matters and creates change

Of the five characteristics, what did the researchers find to be the most important? They determined that psychological safety – "the ability to be bold and take risks without worrying that your team members will judge you" – was far and away the most important ingredient.

Leaders create environments where followers don't see themselves as such. They see themselves as part of something larger, and they feel safe expressing themselves and their opinions knowing that leaders will listen compassionately. Leaders don't always heed the advice, opinions, or recommendations of their followers, but they do take it under consideration when the situation merits. There is no such thing as leaders without followers, and inspired leaders are more collegial and bottom-up oriented than old fashioned top-down, command and control, hierarchical bosses.

## **2. Successful Construction Companies are Great Places to Work**

In today's construction market, the competition for people is hotter than the competition for work. The company with the best team and the most talent can, for the most part, get all the work they want by establishing and maintaining great relationships and generating consistent, first-rate project execution.

To attract and keep the best and brightest, contractors must develop cultures that inspire people via the company's vision, values, and work environment. Good performers want to work with other good performers, and fun people want to work with other fun individuals! Not all great places to work look just alike, but the best form themselves into magnets for good people.

If contractors want to attract great talent, a logical beginning point is to determine what employees want in a preferred employer. The first hurdle, of course, is money. Money is actually pretty low on their list of things based on various surveys and studies. Employees need to make a wage that floats their boat. So if one needs to make \$40,000 a year to pay her mortgage and feed her children, less than \$40,000

isn't going to get it for her. On the other hand, a sum higher than \$40,000 isn't going to produce much marginal satisfaction either. Above the amount where they can pay their mortgage, feed their kids, and basically take care of themselves, money doesn't matter so much. Money is not the biggest determinant.

Beyond money, what do employees want? McKinsey is a huge, multi-national consulting firm, and they did a big study surveying hundreds of thousands of workers. Here are the findings. The first thing employees want is a clear and compelling common vision. They want to know the direction of the company. Where are we headed? Is this company headed in a direction that is consistent with where I want to head as an individual? And does my personal mission align with the company's vision?

The second thing employees want is an open and transparent culture. While we are proponents of open-book management, we are not advocating showing every single line item of your income statement. Some form of open-book management where you communicate with your people and your employees ("Here's where we are. We're ahead of plan. We're behind plan. Here are the corrective actions we're taking"). The key to transparent culture is blunt, forthright communication. Provide reasonable accessibility for your peoples' questions, input, and commentary. Make yourself available and vulnerable, make yourself a part of the team, and be willing and open to communicate with everybody else on the team. Transparency means that there are no secrets. If we have problems, we talk about them. When we have challenges, we discuss how best to tackle them. When we have successes, we talk about and celebrate them.

The third thing that employees want is clear roles, clear responsibilities, and accountability. Some employees don't want accountability, and they may be your worst ones; they want to stay under management's radar. Your good employees, however, want clear roles, responsibilities, and, ultimately, accountability. They really, genuinely want to know how they're doing and how they will be held accountable over time. These three items were McKinsey's answer to the question "what do employees want?"

We would like to add two more things that we've observed. People want to see the impact of their actions. They want to know they are making a difference, moving the needle. If one is an employee among 100,000 others in a huge organization, impact is probably quite difficult to discern. Most construction firms, however, are comparatively modest in size and privately owned. If your question is "why would a super-talented individual want to come to work for me at my small business?" then your advantage, quite possibly, lies in the impact your people will be able to see in their work.

Another thing that good employees want is to be part of a team. They want to know, as top performers, that they will be surrounded with other A players so they can help each other lift the company to new heights. Like great athletes, great employees don't want to be the best player on terrible teams. They want to be supported by other hungry, ambitious people. To the degree you can shape your company to offer these five things, you have an opportunity to be an employer of choice.

Workforce mobility is at an all-time high, and today's workers value and respond to culture more than at any time in our past. Teamwork, purpose, communication, work environment, and the opportunity for personal growth all take on greater importance today than even a decade or two ago. While culture is often subtle and hard to identify, it is the glue that keeps a positive team working happily and harmoniously. It is important for leaders to be purposeful in building and nurturing their company cultures, and having an attractive culture requires leaders to devote time, attention, effort, and money to working ON themselves and their teams rather than simply working IN their businesses. Great places to work are built intentionally – not by accident.

### **3. Successful Construction Companies Have the Ability to Recruit, Hire, Train, and Develop Top People**

Construction is a people business, and there is no greater strength or limiting constraint than having the right people on your construction company bus. As in sports, the team with the best talent is going to win more. Today's employment environment is hyper-competitive for every level of skilled employee. Poaching is the new normal, and job hopping has proven to be an effective way for an employee to get a substantial raise. Culture, as addressed above, is critical to your ability to retain your best and brightest and to defend against outside efforts to cut into your team.

"*Slow to hire, quick to fire*" is a habit that works for successful construction companies. The most successful have a very thorough hiring process to assure candidates have the skills they claim to possess and will fit with the company's team and culture. They use multiple layers of interviews, background checks, and personality assessments to evaluate people on a number of practical and psychological levels. They have well-honed hiring processes to eliminate gut feel as the primary decision factor. Being thorough doesn't mean dragging out the process unnecessarily; the environment is too competitive to expect good candidates to wait for weeks on end for hiring decisions. "Slow to hire" means to be deliberate and process-minded, not to prolong the hiring timeline.

In today's construction marketplace, there are only a handful of proven recruiting and hiring methods: The top tactic is growing from within via formal intern and project engineer programs. Quite a few great companies boast their best results come from home grown talent. In order to develop people internally, leaders must invest in raw recruits and have strong training programs to motivate people to learn and to develop their talents. Identifying and investing in young people who are eager for knowledge pays long term dividends. Be advised that a deliberate, process-driven hiring plan is a long term, patient play and is not a quick fix to fill lead mechanic, carpenter, foreman, or superintendent positions.

A second solid recruiting methodology is an internal referral program. Some employers even bonus employees for persuading others to come on board. This works best where employees already have great company pride and a cultural *esprit de corps*. Pride in the company and its culture drives employees to want to only add other good performers; thus, they are not referring warm bodies strictly for the money. Top employees are potentially great salespeople because they are passionate about your company being a great place to work. And a referral prospect is more easily "sold" because he/she can see how much the referrer witnesses his/her belief in the company and its future.

Some companies have managed to develop a successful buzz in the market as a local employer of choice. Growth is a common denominator for these top recruiting companies – they have plenty of work supported by positive cultures where current employees are pleased to share information and help groom new people. Many develop their cultures by having a great deal of on the job fun layered with after-work camaraderie.

Advertising for talent still works. With a huge number of online channels, an employer can reach people literally across the world! It is lots of work to sort through dozens, if not hundreds, of applications and find great people, but it is well worth the extra effort. Though nine out of 10 construction executives claim to possess great hiring instincts, results simply do not bear this out. Instead of relying solely on gut feel and the fatally flawed, old-fashioned interview, progressive contractors use homework assignments, team interviews, psychometric evaluation tools, and even Google Earth among other things to assure they maximize their opportunities for great hires.

Search firms and recruiters probably have the worst overall track record for successful placement. Part of the problem comes from the fact that usually these head hunted employees leave their jobs for money reasons, and they are just as likely to leave you at some point for more money. The cost of headhunter services can be quite high. In a 3% to 5% net profit industry, paying search fees for multiple positions can be a significant drain. Still, if you need to invest for a specific skill set (such as a travelling superintendent) or just are in desperate need for a body to fill a gaping hole, search firms may produce needed results.

It is most important to hire in advance of need. A successful contractor advised a key factor in his growth was to hire talent “not when it was needed, but whenever I came across it.” He correctly believes that it is easier to build a business to take advantage of a great hire than to find a great hire necessary to fill an urgent need. To accomplish this kind of proactive recruiting and hiring, contractors must cultivate an investment mindset and get over the common construction leader bias to have all people working at 110% capacity at all times!

At the risk of flogging a dead horse, construction is a people business! The most successful companies tend to be excellent in training and development. Again, this requires an investment mindset. It may not be “efficient” to pull all your young field prospects to one job site to witness and learn from a large or complicated concrete pour, but how else can you give them this experience as they rise in the company?

Every single person in your company should have an “individual development plan.” Those who will be expected to fill larger roles in the future need the skills and specific experiences to best prepare. Those who don’t have the capabilities to move up in the organization still need training and development to be the best they can be in their individual contributor roles. People gain pride and senses of accomplishment by increasing their skills and often surprise employers by growing their capabilities and responsibilities over time to a higher than expected degree.

The employee review, a very poorly named and executed process in most companies, is still an important part of an employee’s development. It is an opportunity for them to get feedback on how they are doing and to hear suggestions for improvement. The best companies use the process to manage the continued education and training of the individual and set goals outlining and measuring progress. A best practice is to put the onus on the employee to manage the review process rather than have it be solely the responsibility of the manager (who often doesn’t make time or put sufficient energy into the process).

The construction business is a people business! Keep your standards high. Take your time and don’t compromise when hiring. Make changes promptly when someone is not working out – they may be occupying the place of your next great employee!

#### **4. Successful Construction Companies Have Effective Strategic and Business Planning**

Strategic planning produces better financial, operational, and cultural results over time; it’s that simple. And the results are profound enough to make anyone who doesn’t believe look like someone who believes the sun revolves around the earth. Here are the facts from The Family Business Institute peer members who have done strategic planning at least three years prior to the publication of this paper:

1. Growth rates roughly quadruple industry averages for revenue and profit, and strategic planners even approximately double the performance of our already successful peer members who have not yet adopted strategic planning as a core business function.

2. Collectively, strategic planners have grown 150% from 2012 to 2017 (versus the comparative peers' <sup>1</sup>growth rate of 69.4%). Volume has grown from \$50MM to \$125MM on average.
3. Average profits from 2012 to 2017 grew by 220% (versus comparative peers'<sup>1</sup> growth of 168%). In hard dollar terms, strategic planners grew profits from an average of \$745,000 to nearly \$2.4 million.
4. In almost every instance, the companies in this group established goals via a rigorous strategic planning process, and they proceeded to accomplish or exceed them.
5. Unanticipated benefits of strategic planning are more effective leadership, stronger cultures, and higher morale. Companies that have planned well are poised for even more success in the future.

So, what is it that makes strategic planning work so well? There are eight main considerations that all good strategic planning processes have in common: First, the value of strategic planning is *the process itself*. A good process challenges an organization out of its comfort zone. Great, probing questions from facilitators and company insiders identify barriers that have been holding the company back. Companies find a unifying set of principles and values to rally behind and establish a compelling common vision. The entire organization gets behind the plan and shares in the responsibility for achieving stated targets and outcomes.

Second, once the long-term vision is set, the planning team then establishes specific goals and milestones. Those specific strategic objectives are the building blocks of ultimate success. When contractors add strategic objectives together with values and future visions, a nebulous future becomes clearer and much more realizable.

Third, the planning strategy must provide for organizational growth to stay just ahead of revenue growth. If a company grows without enough good people and the correct organizational infrastructure and support, failure can creep into job results (quality, schedule, safety, and bottom line). Reputation and relationships can become tarnished, and leaders, sensing things are beginning to spiral out of control, pull back the reins at that point. Good strategic planning assures revenue growth is built upon a solid organizational foundation. An investment mindset toward hiring, training, and development replaces the penny pincher mindset to move the company forward. An additional layer of oversight or management support is often needed to sustain additional moving parts and pieces. It is best to keep organizational growth just ahead of revenue growth and to always have the correct resources while simultaneously being efficient and avoiding bloat

Fourth, operations must be solid. Processes must be efficient and consistently applied across the organization as it grows. Growth means having more moving parts to be managed, and that's another place strategic planning pays off. The pure entrepreneurial style characteristic of most construction firms gives way to an increased amount of structure and organization. Finding the proper balance of individual freedom and initiative with the need for management controls will help maintain a great culture and solid business results through the growth period. Having a coherent strategic plan supports the team and provides confidence in a bright future.

Fifth, getting really strategic about what work the firm is going to pursue and how it will pursue it is critical to success. Sustainable contractors have established a clear pathway to success coupled with a clear understanding of how to achieve a well-diversified and profitable mix of work. The best plans are built upon the premise of building lifetime customers and earning their loyalty by adding value. Value is built on great performance; having a capable organization with great people and operational excellence allows customers to rest well at night. Contractors must, via the planning process, determine what differentiates them from the competition and develop ways to increase or maintain that competitive edge to build their business development (BD) efforts around their strengths.

---

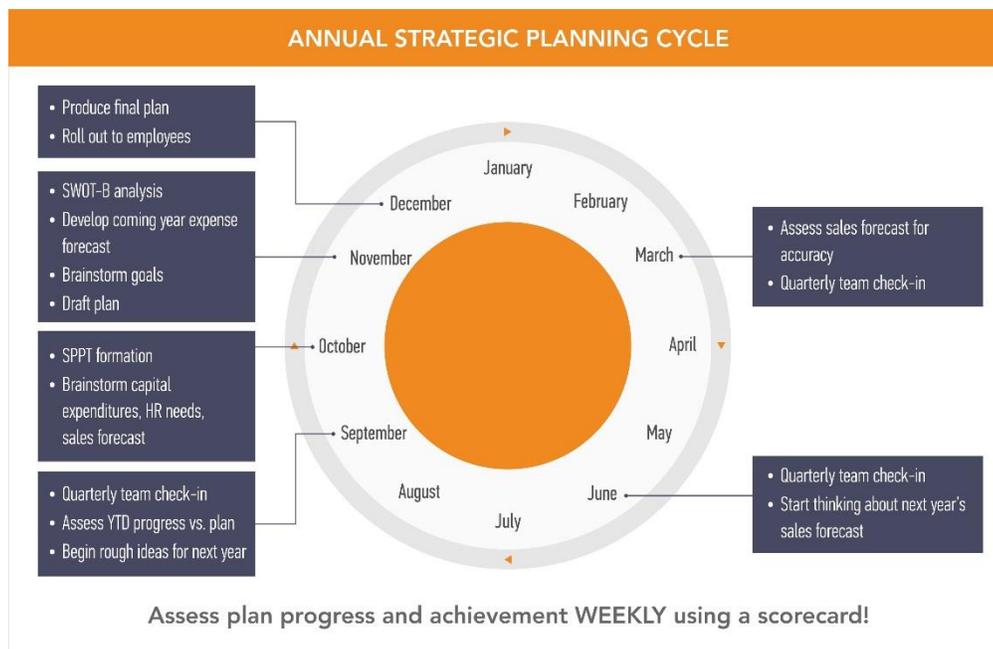
<sup>1</sup> Source The Family Business Institute benchmarking data. See Appendix for more.

Once the firm knows what it wants its customer base to look like, the sixth step is to develop a work acquisition strategy that allows it to meet goals. As revenue grows, the front-end BD machine must be able to sustain growth and assure the desired level of backlog and future projects. It is usually counterproductive in construction to grow rapidly then shrink back to a prior size as this causes organizational stress and personnel disruption. A well thought out business acquisition plan will support healthy, sustainable growth. BD efforts need to be multi-pronged in order to produce diversified work. Different sectors and niches require different strategies, efforts, and structures for success. And a contractor’s work acquisition strategy must fit neatly with its other strategic objectives. Understanding your markets and prospective customers and creating a coherent new BD strategy is a key benefit of strategic planning.

Seventh, strategic plans must be supported by realistic budgets and long term financial forecasts. How can a company execute a plan without being able to visualize the bottom line, gross margins, and other important financial ratios? Contractors complain that they “can’t predict the future” and do long term financial forecasts. This is simply hogwash! Good contractors can and do establish financial and other forecasts, and they produce them in great detail. It isn’t rocket science!

Finally, good strategic plans have solid implementation and accountability plans. Spreading the implementation workload, even beyond your strategic planning team, is important. Contractors must assure that each major task has a passionate team assigned to it. That team must have clear, cohesive execution steps and realistic timelines so progress can be measured and supported. The strategic planning group must meet regularly, and leaders must hold the teams accountable over time. Strategic plans fall flat without leaders who devote time, effort, and passion to holding their teams strictly accountable for real world results.

Successful strategic planning is not a one-time event. The process of implementing the plan should continue throughout the year(s) with necessary adjustments along the way. The graphic below represents a healthy annual strategic planning cycle which keeps plans fresh and updated with the added benefit of keeping leaders and their planning teams fully engaged in execution and accountability.



## 5. Successful Construction Companies Are Effective at Getting Work

It's impossible to perform well, achieve financial targets, or build a great organization unless there is a sufficient flow of work. Ironically, this is one of the most elusive skills for a good construction company to master. Because work can be acquired in so many different ways and through dramatically different channels depending upon the customer sector, delivery method, and regional nuances, business development can be a game with continually shifting targets. Few companies are expert at all methods of project acquisition, but most are strong in at least one primary acquisition method. Let's explore several BD success factors.

The one overarching theme of the most successful companies is that they have at least one niche industry or customer where they have built a strong, abiding relationship. These "lifetime customers" produce significant repeat business and gross profit over time. The keys to the stickiness of these relationships are trust, responsiveness, open and honest communication, and a consistently positive construction experience. While there is personal attention and nurturing required to maintain long term customers, performance is still the final evaluation factor. Poor construction performance outweighs personal attention and relationships every time.

Each great repeat customer starts with a single job opportunity. Top companies are smart about recognizing opportunities in the market and strategizing how to gain them. Having a strategic approach for which opportunities a company pursues is at least as important to success as how one pursues it. With a clear acquisition strategy, BD and estimating efforts can be aligned for greater success and less waste of resources.

If a contractor is brutally honest about it, construction services, like almost any business product or service, are a commodity. Low price is almost always a differentiator. Even when a project is negotiated between long-term project partners, budgets are a constraint, and the ability to get the best prices will impact your BD success greatly.

Great contractors systematically and strategically approach each bid. A great piece of contractor advice is: "If you are going to bid a job, always find at least three unique advantages!" Essentially, they were saying you have to work the bid not just go through the motions and collect numbers like a broker. Find opportunities in the drawings to build more efficiently. Partner with a trade contractor that can help identify advantages. Find a way to break up or combine the scope to your advantage. Find a low sub number nobody else has. Get top superintendents to work alongside estimating to smoke out value engineering opportunities. Determine unique ways to save general conditions versus how others might approach the work.

There are two commonalities among general contractor companies who know how to "get low". First, they maintain and nurture a loyal and broad subcontractor base. To get the best prices, a firm must have good bid coverage so it is more likely to have the best price or value versus competitors in all or most trades. The best treat their subs more than fairly; if subs can achieve productivity on your jobs, get paid faster, and get support for necessary changes, a contractor is more likely to get the coverage and the numbers to be effective at winning work.

Second, they realize that business development is somewhat akin to winning a beauty contest in that choices can be quite subjective. Most construction company owners and leaders are engineers or came up through the operations side of the business; they are usually not natural salespeople or marketers. The most successful companies have invested considerable time, effort, and money and mastered the art of competitive selling themselves effectively. Here are some commonalities of that success:

1. They learn the rules of each game and formulate a game plan and strategy based on these rules. Where there is a scoring system, winning contractors make sure they can score well. If the selection committee has a certain bias, they learn what it is and play to it. The very best get upstream in the process and make sure they contribute to the thinking behind how decisions will be made and influence them in their favor even to the point of providing or helping write the Request for Proposal (RFP). If you have the most schools built in that county, why not have the rules favor those who have built more schools? On the other hand, if the rules are set against you or in someone else's favor, you need to find a way to "appeal to the jury" as a good attorney might do in a closing argument. There is a common adage in construction: "No one ever got fired for hiring Turner!" What this means is, buyers tend toward safe choices. To win against this natural bias towards hiring bigger firms, how can you cleverly position your company as the safer choice?
2. When the biggest of the ENR 400 is in the hunt, a contractor must check all the boxes. Your presentation or qualifying statement must touch on each standard element. You have to have a credible answer for how you handle BIM, job and collaboration technologies, LEAN, pre-con, safety, quality, etc. Don't give the committee any easy or technical reasons to eliminate you from consideration.
3. Differentiate yourself! What do you do better than everyone else? If you can't quickly answer this question for yourself, you will have trouble selling it to a selection panel. The best companies are very self-aware. They know what they do well, and they are very good at communicating and selling that advantage. Most successful contractors have "branded" their advantage. By giving a brand to their processes and systems, they elevate their importance and create a unique asset in the company's BD arsenal.
4. The most important part of any presentation is the team itself. Superintendents probably win more jobs than any other team members, yet many of them are not well spoken at presentation time. The best companies do training, rehearsals, and role playing to help their superintendents and other BD team members shine. Success also comes from having them very familiar with the project itself so they can talk comfortably about their plan, approach, concerns, etc. Putting them into a position to talk about the nuts and bolts of the project versus giving a scripted speech is a superintendent best practice.

Business development people come in all shapes and sizes, and more BD hires fail rather than succeed. There is no single profile, reward system, or one size fits all system for BD success. Some company's ownership groups have BD responsibility; other companies have team leaders who are responsible for maintaining relationships and generating work in specific areas. In any case, having a well-honed strategy, having the right fit for the BD position, and having clear marching orders for your BD staff are keys to success.

## **6. Successful Construction Companies Have a Diversified and Profitable Mix of Work**

Construction is a cyclical industry with ups and downs driven by macroeconomic elements beyond the control of any single contractor. Slowdowns and recessions occur routinely and are driven by different stimuli affecting different sectors of the construction economy. No two recessions are alike in their impact, and there is no way to perfectly predict when or how the next downturn will play out. Independent of recessions, certain movements of industry sectors can have an upward or downward effect on regional construction markets. There is frequently a double whammy for construction in downward cycles as not only does the available work shrink, but, due to supply and demand, margins shrink at the same time. Adding to the challenges, risks can go up due to one contractor's problems rippling across others on the same job.

A good example of regional boom/bust cycles is the shale oil expansion driving up markets such as North Dakota, south Texas, and the Ohio/West Virginia/Pennsylvania areas followed by the sharp drop in global oil prices affecting Alaska, New Mexico, Wyoming, and other markets. Another example is high commodity prices in agriculture helping to insulate the nation's breadbasket from The Great Recession followed by lower prices in recent years which have softened these same markets.

To be successful over time, it is essential to avoid overconcentration and to have a presence in diverse sectors so all your construction eggs are not in one basket. Hotel builders, for example, were subject to a 70% market drop from 2008 to 2011. Industrial contractors at the same time actually saw a rise in available work. The Great Recession saw a drop of 50% in private construction, but federal government work had historic growth through 2011 allowing capable firms to maintain reasonable volumes and margins.

The most successful contractors have profit diversity in their businesses which allows them to succeed in multiple economic environments. Generally speaking, large and high-profile projects bring more and stronger competition and produce smaller gross margins. On the other hand, small projects, niche markets, and ugly or complicated projects will frequently offer less competition and allow for higher margins. Negotiated work based on value propositions offer the opportunity for differentiation and higher margins. If buyers value time, safety, quality, relationship, and/or experience over merely price, there is opportunity to get higher margins. If a construction firm only competes in price sensitive areas, it is hard to gain enough margin to even cover overhead much less make a standard industry profit. Many of the competitive Construction Management (CM) markets across the country offer gross profits that are below even net profit expectations for small and mid-sized contractors who don't compete in the CM world. On the other hand, if a contractor only does small projects or renovations, it is hard to produce sufficient volume for long term profits. Small, project focused companies have a hard time building their resumes to be able to compete on larger and more complex projects when markets demand that work.

Analysis of the most successful contractors show a mix of high margin sectors with lower margin ones and a predominance of relationship - and value - (rather than price) based project acquisition. A growing trend is for contractors to self-perform work or have service entities that further contribute to high margins.

## **7. Successful Construction Companies Have Operational Strength**

Top companies perform! They do most things well in getting projects completed quickly, safely, and efficiently. Top performing contractors show their excellence in some of the following ways.

Effective job cost reviews are the key pieces of oversight in top companies. When problems do arise, the best companies identify them early and mobilize the resources necessary to apply the best solutions to reduce the cost or schedule impact of the problem.

They also have tight and complete scopes of work. When projects come out of preconstruction and move through buyout, there are no scope gaps, they have bids evaluated to be able to make the best purchase decisions, and they solidify both scope and responsibilities in a well-choreographed contract.

They are excellent at project launch. Ideally, superintendents and project managers have had involvement during the pre-con process. If not, the company has an extensive turnover and job launch procedure to assure the project team understands the history, thinking, and conversations that are behind the estimating, schedule, and subcontractor choices. The best construction minds are brought to bear on formulating the construction plan with the input of key subs and parties that will be involved

in execution. Critical path items and obstacles alike are identified and anticipated, and detailed follow through assures the project stays on course throughout its life cycle.

Plans, submittals, and specifications are reviewed thoroughly so that problems are anticipated or identified early when the cost of change is smallest, and opportunities for savings or improvements are identified and decided upon. The people in the organization with the right skills are brought in at the right points in the process to assure time and money savings and maximum value can be extracted from the project.

Excellent construction companies control time. That involves having project management that plans, checks, and double checks to assure the people, plans, and materials are all in the right places at the right times. Superintendents assure that on-site coordination produces efficient results for all project partners. Top companies work with owners, architects, and engineers to assure timely decisions, and parties are held mutually accountable for achieving the project schedule.

Good companies have solid processes. They have well thought out checklists and procedures that are utilized to ensure all the bases are covered in their operations. While all companies have “B” and “C” players, the best have strong methodologies and management support that allow them to consistently deliver “A” level performance from all teams. It takes talent, knowledge, and effort to deliver consistently successful construction projects. Having team members with good technical education and training, excellent management and relationship skills, hands on experience, and a “get ‘er done” attitude is critical.

Finally, great companies are strong finishers. They don’t allow projects to lose momentum at the end. They keep their trade partners engaged through punch list and close out processes. Strong administrative support and organization for close out is another common denominator of operational success.

Construction success means being able to deliver projects safely, on time, and with expected quality while maintaining solid relationships. The basic blocking and tackling can never be neglected, or poor results will submarine the ability to get work and make a profit doing it.

## **8. Successful Construction Companies Have Proper Capitalization**

Having proper capitalization requires a delicate balance between too much and too little, and it is critical to have sufficient resources to fuel business growth in good times or sustain it in lean ones. If a contractor is around long enough, something major will go wrong; it’s inevitable. Owner default, subcontractor default, economic recessions (local, regional, and/or national), loss of a major customer or job, job funds being frozen, poor performance, contract disputes, key employee mutinies, and other conditions beyond a leader’s control can all threaten your company’s success and viability. A contractor must have the resources to outlast or overcome these all too common challenges.

Too little capital has detrimental strategic effects on the business by limiting growth, the ability to hire, reward, and retain the best team, and the ability to pay subs or suppliers sufficiently well to get preferred pricing and performance. And it causes added stress for owners and senior leaders resulting in a lack of focus and too much time sunk in worrying about and managing the details of cash flow versus building and operating their businesses.

Overcapitalized companies, interestingly, tend to underperform their more efficient peers for both financial and operational reasons. Companies with excess and underutilized capital reflect lower Returns on Assets (ROA) and Return on Equity (ROE) simply because the denominator of the ratio is unnecessarily high. What this really means is that a company is underperforming its opportunities – it

could be doing more with the resources at hand. Another way to look at this is that the firm probably has excess cash/cash equivalents/investments that do not generate as much return as the activities of construction. In the current low interest rate environment, these returns can often be 1% or less. Secondly, companies with too much equity and cash tend to be less motivated – perhaps even complacent. Their profit percentages on sales, timeliness of billings, receivables, and payables all tend to lag leaner peers.

There is no precisely correct level of capitalization. Each contractor has a different risk tolerance which is reflected in capitalization decisions. Most successful mid-sized general contractors maintain both net worth and working capital of about 8% of annual revenue. Trade contractors, depending upon type of work and size, will typically keep on hand between 10% and 20% of annual revenues. Bonding and banking partners offer additional guidance or requirements, and these vary depending a contractor's level of personal indemnity among other factors.

A commonality among most successful contractors is that they live relatively modest personal lifestyles - particularly through the “building stages” of their businesses. They prioritize company stability and sufficient capital for growth before spending lavishly. This mindset is reflected in the leadership persona of mature, top performing companies as well. Leaders who siphon money from their companies for personal extravagances often have trouble inspiring their teams to perform. The leader who invests in his company and his team will more likely engender loyalty among followers and create a healthier work environment for everyone's benefit.

## 9. Successful Construction Companies Are Data Smart

The most successful contractors are data smart. They understand their profit models and track profitability by sector, division, and even by project manager and superintendent. They also track and manage job performance on a timely and consistent basis to identify and resolve issues before they become serious and expensive.

Within each company, there are certain drivers of business success. In Jim Collins' book *Good to Great*, the “Hedgehog Concept” asked readers to determine the single economic equation that defines success for their businesses. In construction, that equation might be: **Success = Gross Profit – Overhead**. Pretty simple, right?

Within that equation there are two major variables. The first one is gross profit. Top operators are gross profit oriented instead of revenue oriented. The old adage in construction is “volume kills, and profit thrills!” Rapid top line growth, particularly with thin margins, puts a company at risk. It is important for a contractor to understand which efforts generate the highest returns and then to focus on growth in the right areas. In contrast, less successful companies devote too much energy and focus on growing volume at the risk of margins (and possibly engage in other high-risk activities as well). As mentioned in the work diversity section, it is important to have some high margin niches. Focusing on developing and growing market niches provides the highest returns with the least risk. Keeping a good balance of work allows for sustainable success through economic cycles and even generational succession.

The second variable is overhead. Good operators spend their money wisely and intentionally avoid the expense creep which comes with lax controls and attention. On the other hand, top performers are not penny wise and pound foolish. They invest wisely in the tools of the trade that make their employees more efficient and keep up with innovations necessary to compete and communicate successfully. They invest proactively in talent and IT and assure they are right sized to handle and sustain growth. Successful contractors establish and maintain an electronic “dashboard” of drivers of financial success. This keeps their focus on the right activities, raises warning flags when the ship is veering off course, and provides leaders with insights into how to make needed course corrections.

Successful contractors have solid financial systems with internal checks and balances, timely and accurate reporting, job reviews, and work in process adjustments. Great operators have forward looking tools and detailed forecasts that predict the company's (not just individual projects!) trajectory and allow for organizational planning and adjustments in strategy.

The whole idea of being data smart is to be better able to strategize a successful and profitable business model, to understand early on when any part of the strategy or execution is not working, and to be able to make tweaks or changes to keep the company on a positive course. Data and IT deserve more attention from contractor leadership teams than they generally get, and part of a contractor's success strategy must be the continued maintenance and upgrade of those systems.

## **10. Successful Construction Companies Have Effective Risk Management**

Simply put, successful contractors avoid bad jobs. At the end of any given year, a contractor will have some blend of jobs that performed normally or according to plan, some "dogs," and, hopefully, a few home runs. How this mix of jobs comes in distinguishes a successful year from a bad one. Avoiding dogs and making sure losses are minimal is key; successful contractors have formal bad job avoidance and mitigation strategies. These are like the military's fail-safe defense systems where certain things trigger automatic avoidance or mitigation strategies to assure big problems remain small.

Disaster jobs usually have one or more of the following characteristics:

- Job was very large or a company's largest ever job
- It was the first job of its kind
- It was the first contract of its kind or type
- The customer didn't have project financing in order
- There was a lack of subcontractor performance or even failure
- Rapid growth added stress to already hard-working teams and systems
- Company leaders developed an attitude that the company was bulletproof and could not fail which can blind even good contractors from obvious risks
- Company leaders had achieved "enough" success and had become complacent
- The company had inadequate capital to accomplish growth, succession, or other long-term strategies

## CONCLUSION

Easy to say, hard to do – right? Long term success remains elusive for even the most driven construction leaders, and many times they feel as if they are alone on an island without the support and feedback networks to help guide them along the right path. Please consider these five steps for achieving breakthrough and sustainable success:

1. **Define success for yourself.** What does it look like and feel like? What is the end game? What would make the journey a success? Financial success might be the easiest definitional component, but don't ignore all-important quality of life aspects.
2. **Join a construction industry peer group.** The ability to see and learn from others' successes and failures is invaluable. The support and frank advice of contractor peers is as valuable as any board of directors in existence. Additionally, every peer group member represents a leadership and management "work in process" from which you can learn. Finally, the ability to R&D (Rob and Duplicate) fellow members' best practices can save you years in development of better processes and systems. Peer groups dramatically accelerate contractors' learning curves.
3. **Develop a comprehensive, long term strategic plan.** You likely need a facilitator (especially if you are undertaking strategic planning for the first time or trying out a new methodology) who will challenge your thinking and make sure you have a cohesive plan that is achievable, not just pie in the sky. Even a rudimentary strategic plan is better than none at all, however. Keep trying, and you will gradually develop your strategic planning muscles!
4. **Work ON your business more than IN your business!** This is a hard step for many to take, but it is necessary in order to create sustainable excellence for your organization. If every process relies on you, your company is not sustainable.
5. **Get to work and enjoy the journey!** Each of the "Top Ten Reasons Contractors Succeed" probably offers some areas for improvement in your organization. Vince Lombardi said, "Perfection is not attainable, but if we pursue perfection, we might catch excellence." Let the pursuit of excellence drive all your business decisions.

*Note: Engelbrecht and Rivers want to credit The Family Business Institute consultants John Mayes, Bundy Bundesman, Doug McCright, Bill Provett, John Stump, Mike Flentje, Bill Babb, and the rest of the FBI team for their assistance in developing the content of this White Paper.*

## APPENDIX: Where does The Family Business Institute get all this contractor information?

### RESULTS

The Family Business Institute can be authoritative about contractor financial and performance data because we have collected such a wealth and depth of data from our peer group members over the years. Each peer group member company provides benchmarking data across 400+ metrics versus their peers, the larger peer group program, and a national database of contractors of similar type and size. They also receive compiled historical results and trend analysis on financial and operational performance. When a contractor hosts a meeting, that company undergoes an intensive peer audit which encompasses a deep dive into hundreds of factors that determine success or failure. Each company receives analysis utilizing:

1. Employee and leadership surveys
2. Interviews and evaluation of key team members
3. Assessment of future leadership and succession plans
4. Assessment of systems, processes, and procedures for operational and administrative effectiveness and efficiency
5. Compensation comparisons of key people including owners
6. Peer critiques of all aspects of the company and its leaders

Through this process of exploration, sharing, and brutally honest feedback, members are able to identify success and failure factors and adopt best practices that enable them to achieve their corporate and personal goals. As these successes have accumulated over the last 15 years, it is now possible to define the “how to” behind lasting success.

Peer group members have enjoyed remarkable success over time. For those peer groups that have been together for greater than three years, they have produced the following results:

1. In 2017, commercial and Institutional General Contractors experienced average volume growth of 17.4% versus industry growth (per The Risk Management Association statistics) of 4.3%
  - a. Five-year revenue growth was 69.4% versus the industry average growth of 32%
  - b. Profit growth was 43% in 2017, and five-year profit growth was 168% versus a five-year industry average of only 68%
  - c. For 2017, the average pre-tax net profit was 3.9% with a 40% return on equity versus an industry norm of 3.2% and a 25.7% return on equity
2. Masonry members saw even more impressive results
  - a. 19.7% volume growth in 2017 and five-year revenue growth of 61%
  - b. Profitability was up 31.4% in 2017 and 568% over the last five years
  - c. The masons’ 12% pre-tax net profit was double the industry average for their category
3. Mechanical/Plumbing members grew volume 12.5% in 2017 and 61% over five years
  - a. Profitability was up 3.4% in 2017 and 96% over five years
  - b. Their pre-tax net of 6.9% was well above the 5.2% norm for the industry

	<i>Commercial</i>	<i>Masonry</i>	<i>Mechanical</i>
<i>Five Year Volume Growth</i>	69.4%	61%	61%
<i>Five Year Profit Growth</i>	168%	568%	96%
<i>2017 Pre-Tax Net</i>	3.9%	12%	6.9%

While these are just financial results, they also point to strength in the softer, less measurable characteristics of success: culture, great people, and balanced leader lifestyles. The fact that this success is measured over time points to improving sustainability. And sustainability is characterized by effective leadership, strong values, and a clear, well-communicated vision.