Good morning, everybody. Dennis Engelbrecht with The Family Business Institute, Digging Deeper.

I read a recent article about a study that just came out. I'd seen some prelims of this study, but it was about the COVID-19 impact on productivity in the construction workplace. It was a study that was specifically done for mechanical contractors and electrical contractors. What it basically found was an 18% impact on productivity.

Wow. I mean, first of all, you have to think of this. Construction is an industry where relatively low margins. If you look at the average profitability margin for construction, it's around 4% over time. An 18% effect on productivity when you have a 4% net margin is scary. All right? The other scary part about this is, as contractors, you have 9 to 12 months, maybe even longer, of backlog where you're already contracted at a certain price to do the job. Now, you have this outside impact. We also have contracts that dictate what we can get reimbursement for in terms of changes and things like that.

This presents an amazingly challenging situation for our industry. The first part is, if you think about an 18%, if 50% of your costs are your labor, and you have an 18% impact, that's a 9% impact on your gross margin, which is more than double your net margin. Basically, if you took this average company and you ran with your existing contracts with no changes with this 18% loss, you're under water 5%. Now that, if you think about this, across the entire industry could have a devastating effect. Obviously, some of those people are trying to execute change orders, and things like that, and call on their contract language to get reimbursement where they can, but there are many areas where, where they simply can't.

There are several things that as contractors you need to do. The first is make sure you're measuring your own impacts. Some of these are hard to measure, but if ingress and egress to the job site takes an extra four minutes because you have to have your temperature tank and are you going to fill out this form or you got to do something just to get on and off and that happens a couple of times a day, or even when you go to the bathroom for example, you've got to measure those impacts. Keeping six feet of space is not normal for your trade. You have to measure the impact of that and all the various cleaning and things like that, that have to happened.

First of all, you've got to measure your own impacts if you're going to get any, either reimbursement or even looking forward, if you think of about estimating the next job, "How do I factor this 18% loss of productivity into my estimating on the next job? If I do just add that on, well, how do I stay competitive if the next guy's not adding it on and I have to get low?" That's an amazing channel knowledge for the industry.

The next thing to do after you measure your impacts is to, of course, see if there are any areas for contract recovery and to pursue those. In any case, I think it's important to be strategizing how you can minimize these things impacts. Now, certainly if you're a trade contractor, you've got to look to how you can possibly make up for the productivity impacts that you're having, maybe by requiring your people to arrive on site 15 minutes early so they can actually start on time or whatever various things that you can do with your processes to maintain your spacing or other things that you're doing. We really need, every company needs, to be strategizing how to stay safe, but minimize those impacts at the same time. Then, of course, make sure you're noticing according to your contract, getting notice in that you are accumulating these costs and trying to figure out what these costs are. They're going to be submitted at a later date.

Now, in sort of minimizing those impacts as the general contractor, this is happening across trays. This study was done on electrical and mechanical, but it's happening in masonry, drywall, painting. These same impacts are affecting everybody. You have to be figuring out, well, again, maintaining safety on your job sites. How do you minimize the impacts to all of these trades on here because surely those costs are going to come back to you in one fashion or another? If you're a GC, of course, you need to be prepared for a potential onslaught of change orders, claim proposals, things like that. Make sure that you're noticing promptly and executing out of your contracts.

Some of the real dangers out there as a GC, you may have some subs, either their proposal in on a bid, or even have them under contract and the possibility that that subcontractor may withdraw because, as they look at it today, they might be looking at and say, "Boy, if I actually keep under this price that I've agreed to, I'm going to lose 10%." Well, obviously, they have a legal obligation based on your bid documents, and your contracts, and all of that, but that hasn't stopped folks from walking away from contracts in the past. Just be aware of that risk and of course the chance that trade contractors or GCs that self-perform may not absorb these costs that could even go under based on these additional costs and having to execute on contracts that they've signed some time ago. Again, you've got to be watching for potential bankruptcies or companies getting in trouble to make sure that you've got a contingency plan and how to continue executing on your project.

Then finally, I talked about figuring out how to account for this in estimating, but you also want to make sure that you're executing on your buy out even more quickly than normal. If you've got bids in, get them to contract as soon as you can before anybody has a chance to withdraw or walk away. Also, as GCs possibly requiring more surety bonds is one way to protect you as you go down the road.

Then I'd say also just be aware of a general risk to the industry. Even in the past several years, because of our sort of overcapacity nature of the industry, costs for construction has been rising. Now in the last six months or so those costs have started to level out or come down, but if we have an 18% impact on productivity and you factor that across the entire industry, that is a potential driver of higher construction prices again. That could weaken demand or impact the ability of projects that are in pre-construction, actually get them within budget and get them into construction. Lots to think about here but look again within your own company and see where this potential 18% impact on productivity is going to hit, how you're going to account for it, how you're going to protect yourself as you go forward in that environment.

Again, Dennis Engelbrecht, Digging Deeper. Thanks for tuning in.