

Why Contractors Should Always Prepare for the Next Recession.

By **Daniel Huckabay**, President, Commercial Surety Bond Agency

I met with one of my business mentors the other month, and in addition to the normal annual budgets I create for our business, he asked me to prepare a projection assuming our revenue declined by 30%. He asked me to outline the things that I would cut in order to remain profitable and give thought to how long it would take to shed some of the overhead.

optimistic people – otherwise, we probably wouldn't have the fortitude to get up every day and do what we do. That being said, remaining vigilant and disciplined in all areas is incredibly important even during an upswing in the market. The exercise my mentor put me through reminded me of two important concepts.

The first concept is regardless of where the market is



My initial thought when he asked me to do this was, “Why would I want to do that? Things are going great and by all accounts the market will hopefully improve over the next couple years.” As I went through the exercise and thought about it more, I could see the wisdom in what he had me doing.

Most business owners by nature are relatively

today, there will eventually be another recession. No one can predict exactly when, but one thing we can all bet on is it will happen. It may sound obvious talking about it here, but I would argue that the thought typically fades down into the dark caverns of our minds when things are going well and we're focused on the goals we've set out to accomplish. It's important to keep cyclical reality of the world we live in at the forefront of our minds at

all times when making decisions regardless of the state of the market.

The other thing I got out of the exercise is to remember that during a growth period companies need to be cautious about the overhead they add. By remembering that good times don't last forever and one day overhead may need to be cut, I think it will make me personally more cautious and to think critically about the overhead I do add.

In an ENR article written by Dr. Thomas Schleifer, a construction expert and professor at the Del E. Webb School of Construction at Arizona State University, he talks about the same concepts for contractors. He goes on in the article to say, "Every category of overhead expense should be scrutinized regularly, and overhead costs should be adjusted at least annually in anticipation of next year's sales." Therefore, rather than chasing volume to cover a consistent level of overhead, Dr. Schleifer encourages creating as much flexibility in your overhead as possible to adjust it to your projected sales when sticking to your core market. This can be

done in a variety of ways but include things like renting equipment instead of buying with debt that needs to be serviced; using outside consultants to fill positions like accounting, project scheduling or engineering; securing office space in a multitenant location that can be expanded or contracted; and putting in compensation structures more heavily weighted on profitability.

Every business has to make decisions that fit their particular profile, and some will argue that approaching business in this fashion will increase their costs. This certainly may be true during the good times, but the ability to shed the overhead quickly during bad times will lead to greater profitability. While every company will have ups and downs, I can tell you that the business owners we work with that have the greatest net worth have the least amount of variability in their profitability over the lifespan of their business. One of the main characteristics that Warren Buffett looks for when buying a company not necessarily whether they had the biggest profit in any given year. Rather, he looks for consistency over many years. ■



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