

# BENCHMARKING

## Corporate Performance for Contractors

By Jerry Jackson and A. E. (Lanny) Harer

**B**enchmarking is a valuable management tool for improving your corporate performance. Whether you want to set improvement targets based on your own history, improve your processes by learning from others or aim for performance levels achieved by the best in the business, benchmarking is your vehicle.

The greatest value that benchmarking can bring to you is direction. A complete benchmarking program can tell you where to go and how to get there.

Three general categories of benchmarking currently exist: performance benchmarking, process benchmarking and self-comparison benchmarking (also called baselining). Let's examine the differences in these tools.

### **Performance Benchmarking**

What is the average fee produced per

project manager in your company? Is the productivity of your estimating staff measured in dollars, numbers of jobs or a higher fee than that of the average contractor? How many dollars as a percentage of contract revenue or fee do you spend on your project control system? What are your general accounting costs as a percentage of fee or revenue? Are your safety costs grossly out of line with those of your competitors? Do you generate a high return per position throughout your company? Does it matter if 25 percent of the contractors in the performance benchmarking database perform better than your results? Which of these measures have high correlation with profitability in highly successful companies in your industry sector?

Literally hundreds of factors and relationships can be measured and benchmarked in a contracting organization. The factors measured are often called "metrics" by benchmarkers. In the vari-

ety of benchmarking databases managed by FMI, management consultants to the construction industry, FMI tracks more than 100 benchmarks for each construction industry sector's database base.

First in the process is identifying the most profitable 25 percent of the participants as Best-of-Class performers. The metrics of those Best-of-Class performers are tabulated for comparison to other participants, allowing these participants to perform gap analyses. Further, those performance metrics that have high correlation to profitability are determined, allowing identification of critical success factors for various industry sectors. Finally, by substituting certain Best-of-Class metrics into the participant's financial model, the potential value of performance improvement can be estimated.

The value of performance benchmarking lies in the direction provided by the

benchmark, as well as in the worth implied by the difference between the participant's performance and that of Best-of-Class performers. Performance benchmarks help you keep your focus on results: both your own performance and that of Best-of-Class performers. Performance benchmarks can spur you to strategy revisions or profitable reengineering of your business processes as you seek to match or exceed Best-of-Class levels.

### **Cautions**

Some caveats are in order.

First, ratios can be misleading. For example, a high return on investment can be produced by a highly profitable contractor or by a marginally profitable contractor who lacks capital.

Second, most performance comparisons should be with firms performing somewhat similar work. Other characteristics such as size, location, nature of contracts, etc., all have bearing on performance results.

Third, differences in definitions between you and the source of the benchmarking standard may lead to wrong conclusions. In certain metrics, you may infer that you should cut your overhead investment to meet a Best-of-Class benchmark based on overhead compared to contract revenue. However, by simply changing the manner in which you cost or seek reimbursement for certain expenses, you can dramatically affect your ratio without a material change in operations.

Finally, by focusing on only those ratios where you compare favorably, you may determine that you already

are a Best-of-Class contractor . . . and fail to push for creative and continuous improvements.

### **Process Benchmarking**

Since every contractor has the opportunity for continuous improvement, process benchmarking may provide some of the improvements you seek. Process benchmarking aims to provide the best practices for comparison to your own, without regard to industry. Process benchmarking is much harder to perform than performance benchmarking. The difficulties are several: selecting those processes you wish to bench-

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mark, finding a reliable source of benchmarking data, comparing processes of dissimilar industries and profitably adapting those practices for your company.

Process benchmarking requires more discussion among participants than is required in performance benchmarking. Rather than focus on results, process benchmarkers examine the systems and procedures of high-perform-

ing companies. From these discussions and observations, process benchmarkers aim to emulate the Best Practices of those high performers. The processes being benchmarked are often processes from firms in industries quite different from the benchmarker.

For demonstration, what would your company's scores be on planning, marketing, internal communication and project control? Using a scale of 0 to 3, with 0 as poor and 3 as excellent, FMI's 75th percentile contractor might show a 2.6 on planning, a 2.4 on marketing, a 2.4 on internal communication and a 2.8 on project control. Differences in your scores and those of the benchmark are more than just numbers.

They may be causal in your profit shortfall against Best-of-Class performers. Of course, these are only four of some 50 management practices benchmark that FMI maintains. These examples only indicate areas for concern and do not directly provide ways of remedying the situation.

Process benchmarking helps you focus on process quality improvement. With benchmarking partners or consultants who are subject matter experts, you can identify specific means of improvement. Although process benchmarking can be quite subjective, good benchmarking practices reduce the degree of uncertainty as to which process changes will be most effective. Process benchmarking is

not a quick-fix. It is a time-consuming process that can ultimately be well worth the time investment required.

### **Self-Comparison Benchmarking**

Baselining or self-comparison benchmarking is the easiest benchmarking to pursue. While low in cost, the primary benefit of self-comparison benchmarking lies in your ability to celebrate improvements.

Since the comparison base is limited to yourself, little impetus to dramatic improvement is likely to be found in this self-comparison. Also, process changes or practice improvements are

dependent on your self-judgment. Finally, because the database is limited to you, quantitative analysis of cause and effect is quite limited.

While limited, every contractor should perform self-comparison benchmarking on a number of metrics. One of the most intriguing baselines lies in the value per employee metric. What is your gross profit per employee? What was it last year? The year before? How have your human and equipment investments improved your value-per-employee benchmark? Or, have your management practices reduced your value per employee? This particular benchmark can be used in a variety of ways, including serving as a measure of the value of additional overhead investment. Conventional wisdom instructs

us to minimize overhead as a percentage of sales. Instead, some contractors have found that by spending more overhead dollars, gross profit and gross profit per employee have increased.

### **Linking Benchmarking Types**

If you are not now performing internal, self-comparison benchmarking, get started. If you seek direction and motivation from Best-of-Class comparisons, get involved with performance benchmarking. If you are looking for process improvements, begin process benchmarking with a focus group, benchmarking partners or a benchmarking consultant who maintains a broad database of process benchmark.

Benchmarking is an important tool for both strategic and business planning, continuous performance improvement and total quality management, or business process reengineering. Use benchmarking to help build a more profitable future for your company,

### **About the Authors**

*Jerry Jackson* is president of FMI, management consultants to the construction industry. He specializes in providing consulting services in business and strategic planning, benchmarking, organizational studies and compensation issues. *Lanny Harer* is a senior vice president in the Corporate Planning and Evaluations Group of FMI. He specializes in implementing business plans and strategic plans for contractors of all sizes. 