HOW TO HARDSCAPE

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Table of Contents

Where to Start with a Budget

Your budget is the roadmap to profitability in your year or season ahead. It is the foundation to building a successful business. If you are not budgeting for your year, you are likely not running your business efficiently and ensuring that each project is being quoted properly to ensure you are recouping your costs and profitability. This is a common way that people go out of business as they do not know how to effectively price projects to stay in business for the long term, cash flow runs out, and they eventually run themselves out of business.

This does not have to be the case with your business if you begin each year with an updated budget that outlines where you want to take your business. It is a great way to create a plan for your business and set goals as well so that you can begin saving for these goals with every completed project and to have confidence on the financial side of your business.

A budget is not a difficult thing to create and is most definitely the one thing that is going to set the stage for your season ahead. Knowing why budgeting is important for business is the first step in realizing why you NEED to be creating a budget in your business. Besides being in more control of your business with a budget, you will find that there are numerous advantages to creating one. It will help inform decisions and decide how you want to grow your business. There is no longer a guessing game when you have a budget, but everything is now on paper and decisions will become much more clear and based on financials rather than guesses or intuition.

Why Create a Budget

1) Goal Setting

The yearly budget sets goals for your business and helps you achieve those goals in your business. It provides an action plan as to how you are going to achieve those goals. As you sit down and decide what pieces of equipment you want to purchase, what your financials look like the previous year, what changes you want to make this year, what employees you want to hire, and what employees will get raises or benefits, you can include these in a budget to ensure that when you create a quote for a project based on your budget that you are making back these costs so you can be rest assured that your business is operating for the long term.

2) Confidence in Pricing

The budget will give you confidence in your pricing, knowing that you are charging exactly what you are worth and not overcharging or undercharging your client. This means that if a client comes back and asks you to drop the pricing for whatever reason, you can confidently tell them that your price is your price. There is no

negotiating. Otherwise the money they negotiate from you is coming out of your profit or your own salary.

The budget sets the stage for your estimating or quoting, as well as your job costing where you can evaluate after a job is completed. This is an important step in evaluating your financials and deciding whether or not your actual numbers from the project match up to the estimated or quoted numbers to that project. This is a crucial step to do during long projects and especially at the end of each project. It will help you decide where things went wrong and where things went right in your estimating and the efficiency of your crew on the job site. It helps you make decisions on employees, equipment, and the direction of your business. And it all stems from creating your budget.

3) Decision Making

Budgeting allows you to make decisions in your business wisely and in the areas that require the investment in order to grow. Choosing where you want to hire a new employee to improve sales growth or on site efficiency is decided in the budgeting process. As is deciding what pieces of equipment you are going to purchase in the coming year. All of these costs need to be inputted into the budget. There is no such thing as saying that is the cost of doing business. Every cost that your business accrues should be in the budget so that you know you are making that money back.

4) Net Profit

The budget also helps account for your net profit at the end of every single year. This profit margin is included at the end of each quote and is included in the budget. This percentage is what you are aiming for at the end of each job after all expenses, materials, labor, and owner's salary is paid. Do not get confused with net profit and your own salary. Those are two very different things.

CREATING A BUDGET

Budgeting for a small business in the construction industry for contractors that are estimating and quoting projects begins with separating and identifying the costs that come with operating the business. These are direct costs to a project and indirect costs associated with your business. Oftentimes the direct costs are easy to include in projects and include things like labor and material costs, but the indirect costs are overlooked and are what kill businesses.

When it comes to creating a budget, you will want to start with a company wide budget and as your company grows to include other services / divisions, you will want to have a budget for each of these. For example, if you start in maintenance and add hardscaping to your business you will want to have a budget for each of

these divisions in your business especially if you have separate crews dedicated to each of these services. Try not to duplicate costs between the two as much as possible. For example, if rent is paid for a shop you should not include 100% of that in each of the budgets, rather you should include 50% of that between the two budgets. The same goes for equipment that may be shared between the two divisions and other indirect and direct costs.

Divisions will have different overhead and labor to sales ratios. For example, installation of hardscapes will likely have higher overhead to sales ratios when compared to maintenance that will likely have higher labor to sales ratios. This means that installation work will likely carry more overhead expenses such as equipment, but maintenance work will involve less equipment work and more labor. However, this will vary from business to business and where the business is at in their timeline.

Creating a budget begins well before the year or the season in which services will be quoted. This is because you want to set your goals prior to the beginning of the period and that your quotes and estimates will be based on the budget. Ensuring that you are quoting and estimating correctly requires your budget to be in place. It will need an overhaul annually and updated quarterly as you see fit to pivot in your business or make a change in your business that would require some adjustment in your budget. For example, a piece of equipment needs to be added, a new hire that was not accounted for, or you begin renting a storage facility / yard.

When it comes to budgeting for your season, it begins by identifying how many hours you have available to you in one season so that you can create an hourly / daily / weekly / monthly / season target in terms of time you have available to make the money you need as a business. This is an easy calculation of deciding how many weeks you have in your season, how many working days in a week, and how many working hours in a day. Multiply these together to get the amount of working hours you have in a season. If you have more than one crew, then you can divide the Overhead Expenses by the number of crews you have and just include all of the tools and equipment your business owns into one category. That way you're making back all of the Overhead Expenses between those two crews.

This only works if those crews are fairly similar in the work that they do. If these two crews do different work for example one does installs and the other does maintenance, then there should be two separate budgets created for this business with the equipment and tools they use separated to ensure these two divisions of your business are making back their costs that they have.

Time

To begin this budgeting process, you will need to calculate how many working hours you have available during your working season. To calculate this, you should determine:

1. Number of weeks in your working season.
2. Number of days per week your crew works.
3. Number of hours per day your crew works.

Multiplying these three numbers together will provide you with the number of working hours available to your business. It is important to not over-budget this number. For example, if you believe that you can work 7 days a week and put in 12 hours, but in reality you only get 6 days of work in and work 10 hours per day, then you will be out of money at the end of your working season because of these lost hours. Budget the time correctly based on last year's numbers or based on a normal working week.

Total Number Hours Budgeted =
Working Weeks in Season x **Working Days per Week** x **Working Hours per Day**

You should know that you will need to budget in the overtime pay for your workers and this will be budgeted based on these numbers. This is calculated by taking the number of hours per season that are available and subtracting it by the number of hours your employees can work in that season before overtime is paid. You will need to then take that time and multiply it by the wage of each employee that you are budgeting for them working overtime in that coming season. Then, multiply that by the overtime multiplier that you pay minus 1. For example, an overtime multiplier of 1.5x would be 0.5x that number. Because you are already paying their full wage in the hours that they will work, we only want to calculate that overtime pay which is why we only want the 0.5x and not the full 1.5x.

With the total number of hours that you have budgeted per season, you now can divide the total cost of your yearly expenses by the total number of hours to provide you with an hourly cost for your overhead expenses that should be billed in to every project based on the amount of hours that you will have dedicated to that project. This is how to calculate overhead rate in construction.

Overhead Expenses per Hour =
Yearly Overhead Cost ➗ Yearly Budgeted Hours

Overhead Expenses

Overhead budgeting begins with identifying the indirect costs in your business that are not associated with any one specific project. These costs are paid out by the

business regardless if they are working. Even if there is a day off, the business is still paying for these expenses. Sometimes they are quite obvious and other times they are a little more hidden and you need to really think about where your business's money is going. These expenses should be budgeted for at the beginning of the year and billed out in every estimate based on the amount of hours spent on that project. We will get into more of that later.

There are numerous examples of this from equipment costs, tools, and any expenses associated with those that will be used on job sites to less obvious examples such as rent you pay for your office space or yard, interest paid on assets, professional fees like lawyers and accountants, and marketing costs. These all get added up and budgeted accordingly. Simply put, *Total Overhead Expenses* ➗ *Hours per Season* is how much you need to make per hour just to cover the indirect job costs of owning and operating your business.

When it comes to calculating Overhead Expenses, some are easier than others. For example, rent is an easy calculation because it is a set price every month for that year. Though other costs like marketing need to be budgeted for. Typically you can take a certain percentage of your forecasted revenue or profit to allocate towards marketing or you can look at what you spent last year and decide how much more you will need to market in order to hit your sales goal for the current year. For example, if you plan to increase sales by 15% you are likely going to have to increase marketing by that amount as well in order to drive more leads that will inevitably bring in more sales to your business.

EXAMPLES OF OVERHEAD

Pretty much anything that costs your business money outside of the cost of materials and labor can be categorized as an overhead expense. Overhead charges in construction can include a wide variety of things including:

- Rent
- Accountant Fees
- Lawyer Fees
- Cell Phone Fees
- Online and Offline Marketing
- Insurance - Workplace and Business
- Office Supplies
- Banking Fees
- Software
- Utilities
- Taxes
- Interest
- Software

- Education
- Travel and Entertainment
- Bad Debts
- Investment
- Overtime
- Anything that costs your business money outside of materials and labor.

There are other expenses that can be treated as Overhead Expenses when incorporating their costs into projects. This includes things like vehicle expenses, equipment expenses, and salaries. All of these expenses you know or can budget for what they are going to cost you throughout the year which will allow you to build their costs into every project based on the amount of time that you will spend on that job.

Equipment

Equipment costs are calculated a little bit differently when it comes to incorporating them into your budget. Equipment needs to be replaced eventually, but you do not want to wait until it needs to be replaced to have to make up the money to purchase a new piece of equipment. This is why even though you own a piece of equipment, you should be charging for it on every project to have enough money saved to purchase a new one by the time it needs to be replaced.

To do this, estimate the cost of the truck you want to purchase, estimate the number of years you will get out of the truck, subtract the resale value after those years from the price you pay, and divide by the number of years usage you will get out of it. This is the cost per year for that truck which will be your overhead expense. This can be repeated for all equipment in your business.

Equipment Cost =
(Purchase Price - Projected Resale Value) ➗ Years of Projected Use

In this formula, you are taking into factor the depreciation on the asset with the projected resale value of that piece of equipment. You can estimate the years of use and projected resale value on the piece of equipment by visiting a classified ads list of equipment and seeing what the going price range is especially for your model and how many years of use that piece of equipment has.

Once it is paid off, do not remove this equipment from the budget. As years increase on equipment, payments will eventually come to an end if you finance it, but maintenance costs of that equipment will increase. Eventually it will become so costly in labor and materials to maintain a piece of equipment that you will likely prefer to replace it. This can all be accounted for in your budget.

If you plan to purchase something years down the road, it never hurts to begin adding it to your budget now. This will help you accumulate the price of that equipment so that when you are ready to make the purchase, the money is sitting there for you on the day of purchase rather than having to take it directly out of your profits.

Overhead Recovery

What is a good construction overhead recovery percentage per job? This is specific to every business. Those with smaller operating costs and not a lot of equipment will have lower overhead expenses per year. However, these businesses will likely be taking on smaller projects so likely their overhead costs are of a similar percentage as a larger company with higher overhead costs taking on a larger project. In each of these scenarios, the overhead expenses may take up 25% to 33%.

There are several different ways that we can recover the overhead that is associated with our business. Two ways that are typically embraced are the *single overhead recovery system* or the *multiple overhead recovery system*.

The *Single Overhead Recovery System* is an easier to manage system that applies the same markup to all things when quoting or estimating a project. That means in order to recover overhead, labor and materials are both marked up at the same amount. This markup is calculated by discovering the percentage overhead to total job cost and applying that markup to all things that are being billed out. Though it is easier to manage, it is not accurate and does not quite make sense to apply the same markup to every aspect of a quote or estimate. For example, labor versus subcontractors should not necessarily have the same markup. Labor that is managed by the company costs significantly more than a subcontractor does. Therefore, your own labor should have a higher recovery percentage than that of a subcontractor, but in the single overhead recovery system they will have the same percentage markup. This can also be applied to materials for a project. If you are a hardscape / softscape company, you may want a higher markup on softscape materials because they are more likely to require replacement / warranty work than that of hardscape materials.

The *Multiple Overhead Recovery System* is not quite as easy as the single overhead recovery system, but it is more accurate as it applies various markups to the different aspects of quotes and estimates. Labor is evidently something that requires much more work to manage including administrative tasks that go into payroll, scheduling, and more. Though materials do not require this same work as they do not necessarily require storage or other administrative tasks as these are carried out by the supplier. Therefore, labor would have a higher markup than that of materials in the multiple overhead recovery system. This is why we recommend using this method of overhead recovery.

A budget can be created to discover the amount to which you would need to apply this recovery rate. This requires you to add up the total amount of overhead that you have to recover for that given year in order to be able to apply that overhead to every project that you quote and estimate. When you add up the total amount of overhead by breaking down every cost in your business that is not associated with a specific project as previously discussed, you can then divide that overhead amount by the hours you have available to you in the season. This is the amount of overhead you need to recover per hour in a working day (not man hour).

Overhead Recovery per Hour =
Yearly or Seasonal Overhead Total ➗ Working Hours in a Year or Season

You can then use this to apply to every hour that a project will take up to calculate that overhead recovery into your project while also applying markups to your labor and materials in order to recover costs associated with those which will be covered later.

Employee Costs

Labor is a major part of any project in this industry. It can be reduced with adding equipment, but it cannot be taken out of the equation entirely. There are also hidden expenses that come with hiring labor. Some as obvious as the taxes that we as employers pay and some less obvious like the time we take training them before they become efficient and the turnover that may occur before finding a quality candidate.

When it comes to forecasting employee costs, you can base it off of previous years or a plan as to how you will start your business. This all begins with setting a sales goal for the year that is attainable. From there, you can work backwards from that number to decipher how many crews you will need to achieve that sales goal and how many people in each crew.

For example, if you are looking to double your sales from last year you are likely looking at doubling your number of field employees. You will also want to account for raises that you have set in mind for employees for the upcoming year based on their career trajectory. However, this may also mean that you will need to expand non-labor producing employees such as office staff, a designer, or sales person. These are employees that do not directly produce the end product, but can become crucial as you continue to grow your business.

Will you be able to fill the roles required to be able to expand in the budgeted year to meet your sales goal? Perhaps you are too ambitious with your sales goal. Or

perhaps you can use the labor that you have already hired and invest into more productive equipment in order to meet that sales goal. Maybe you can turn a crew of four into two crews of two with the addition of equipment that you did not have before to increase efficiency.

This is why budgeting is so important to the process of your road map to success as a business. This is the start to planning your year ahead and knowing where to put your money to prepare for that year in order to hit your goals.

Owner's Salary

This is the number one thing I see missed from any budget. This is because many people think that the owner makes what the business makes. The sooner you can think of yourself and your business as separate, the better you will be financially both personally and for your business. You should be paying yourself a salary. The business makes a profit. You can choose to pay yourself those profits as well or do whatever you wish with those profits, but they should be completely separate for the purpose of building a budget and for the operation of your business.

Your accountant may tell you to pay yourself a reasonable salary based on your market value as this is typically what any tax agency may look at if you ever get audited. They may also tell you to pay as little as possible and to pay the remainder as owner's draws from the business. This is not advice and you should discuss this with an accountant. Regardless of what or how you are paying yourself, you should be including a reasonable salary based on the roles that you take on in your business in your budget. If you are not doing so, you are cutting yourself and your business short with every quote that is going out the door.

Write down all of the roles that you fill in your business and how many hours per week you take on those roles. Likely if you are just starting out or are an owner / operator, you are taking on numerous roles but in a part time capacity. For example, you are a salesperson, designer, foreman, laborer, bookkeeper, accountant, and so on. But you are none of these things in a full time capacity other than the roles you fill in the field.

You can then begin to break these down and find salaries online for your market to decide how much you would be paying someone to take on these responsibilities in your business. For example, a full time bookkeeper may be $60,000 per year but you are only putting in 8 hours per month bookkeeping. At 160 hours per month for a full time position you are only filling 5% of that time which would mean $3,000 of that per year salary. Alternatively, you could look at what it would cost to outsource bookkeeping to a firm and include that cost into your salary instead. In doing so, when you finally do decide to outsource this, you are already accounting that into

what you are taking on and your price does not change. The only thing that changes is in your budget you are moving money from your salary to an overhead expense.

Continue this process with each of your roles and responsibilities in your business to be able to come up with a number for your salary that you can include in your budget as a salary. This is treated similar to that as an overhead expense and the calculation will be discussed later.

What this does is it helps you charge your market wage that you are worth in every quote. It also ensures that if you ever get injured, you could at the very least begin to outsource or hire people around you to take on the work that needs to get done without being under water with expenses because those costs are already accounted for.

Additionally you can think about the salary that you need based on your personal requirements. Try creating a personal budget to establish what goals you want to meet in your life and how you are going to get there. Decide where you want to be in terms of your own salary through this. Add up your rent / mortgage, food, essentials, and your own savings. This is the bare minimum and should be where you are at or above right now in your business. The leftover can be reinvested into the business or elsewhere.

Hourly vs Salary

Continuing with discussing the owner's salary, you also need to separate your employees between the hourly wage earners and the salary employees. Those employees that earn salaries will be factored into every project much like an overhead expense would. This formula would involve calculating the number of hours available to work per season and dividing that into the employee’s salary to provide the amount per hour that you should be budgeting into each working hour on a project.

Salary Expense per Hour =
Salary ➗ Yearly Budgeted Hours

Now, this number should be divided by each operating crew that you have in a specific division. For example, if you have two projects on the go at any given moment and have two crews operating, you will want to divide this number by two for every estimate that is sent out. This is because you do not want to be gaining back 200% of the salary, just 100% of the salary. In a two crew scenario, each crew would recover 50% of that salary. It would be nice to recover 200% of that salary, but you would likely be overbidding projects and not landing as many as you would like.

Hourly wage earners are much easier to factor into each project as their hourly cost is calculated into the project based on the amount of hours being budgeted for that project. There is a little more to this than just calculating the wage that each of these workers earn, for both salary and hourly wage workers.

OVERTIME

Overtime is calculated as a budgeted amount and included as an overhead expense that gets billed into every project. This is because overtime is not always predictable, especially in the estimating process for a project. It is easier for you to budget a certain amount based on the amount of hours that you are budgeting for your workers and how much they are paid for overtime.

At the beginning of your working year, you should calculate the total number of hours that you are budgeting for your working season.

Total Number Hours Budgeted =
Working Weeks in Season x **Working Days per Week** x **Working Hours per Day**

With this number, you can then calculate the amount of hours that are paid overtime by calculating the amount of hours per season that a worker can work without overtime.

Total Workable Hours Without Overtime =
Working Weeks in Season x **Working Days per Week** x **Working Hours per Day Before Overtime is Paid**

You can then take these numbers and subtract them to provide the total amount of hours that are overtime payable to your employees. You can use this number to multiply it by their wage and then multiply it by their overtime rate minus 1. For example, an employee that works 100 overtime hours per season and earns a wage of $15 per hour with an overtime rate of 1.5 times (time and a half) would be calculated as: 100 x 15 x 0.5. This would only be for that specific employee and this would need to be calculated for every employee that would earn overtime pay.

An alternative method to this would be to look at last year's budgeted overtime and decide whether or not you would want to increase that by a certain percentage based on employee's wages increasing and the amount of overtime hours that would change.

VACATION PAY, BONUSES, BENEFITS, PAYROLL TAXES, INSURANCE

For employees with salaries, you should calculate these costs as a yearly amount and include it as an overhead expense much like their salary would. This overhead expense would then be included into every project that is estimated.

For employees that earn an hourly wage, you could calculate these as an hourly amount and add them into their hourly wage that would then be calculated into every project depending on the amount of hours that the project is estimated for. Alternatively, if you do not have these as an hourly amount you can incorporate them as an overhead expense much like you would do for a salaried employee.

LABOR EFFICIENCY

Labor efficiency is an important calculation to make when budgeting the amount of hours that a project will take which in turn affects the amount of labor costs for both wage earners and salaried employees, as well as the overhead expenses, that are built into the estimate. That is why this is such a crucial calculation to include.

We calculate labor efficiency as a percentage that would cause the total amount of hours budgeted for a project to increase by. We factor in two things:

1) Driving Distance

This number will change from project to project and depend on if your crew arrives on a job site or comes to your shop first and then drives to the job site. When does your employee start and stop on the clock? Is it when they arrive at your shop and end when they arrive at your shop? If so, this driving distance needs to be incorporated into the working day. If they clock in and out when they arrive on the job site, you do not need to worry so much about this portion. These trips should be added up and included as an hourly amount.

2) Lunch and Breaks

During lunches and breaks, your employees are not working which means it should be factored into the efficiency of their work. These lunches and breaks should be added up and included as an hourly amount.

Your efficiency factor is based on the amount of hours you have budgeted for each working day. You should divide the amount of hours that the above two factors provide by the number of hours budgeted in the working day and multiply that by 100 to provide a percentage. You would then multiply that percentage by the total hours budgeted for that specific project and add that to the total hours budgeted for that project.

For example, if it took your crew 0.5 hours to get to the job site after they were clocked in and the same amount of time back to the yard at the end of the day and took 1 hour of breaks and lunches throughout the day and their working day was 8 hours, the formula would look like this:

2 Hours of Lost Time ➗ 8 Hour Work Day x **100**
= 25% Efficiency Percentage

You would then need to multiply your time associated to the labor portion of this project by that efficiency percentage unless this efficiency is already factored into your production rates. 100 hours dedicated to a project at a 25% Efficiency Percentage (100 x 1.25) would equal 125 billable hours for that project.

LABOR BURDEN

With your total labor time based on the amount budgeted for the project and factoring in the efficiency of your crew, you can then calculate the amount that your labor costs by simply multiplying this time by the wages of the employees that will be assigned to the project and the salaries of everyone on staff. With this number, you can then factor in the Labor Burden.

Labor burden in the field of construction is an invisible cost associated with labor. There are many costs that we have discussed previously in this post that we have factored in as an overhead expense or have added it to the employee's hourly wage. However, the labor burden takes into factor the more hidden costs associated with your employees.

These factors primarily include the cost of training new employees which would be associated with the loss of efficiency for the person training and the learning curve associated with training a new employee until they reach optimal efficiency. Not to mention that not every employee will be as efficient as the next.

This is a difficult factor to calculate, but necessary to include in your labor rates. This can also include any markup amount that you would want to include on your labor.

Cost of Sales

Cost of sales items include anything that is left on the job site that contributes to the final product for the client. That means things like materials and delivery, rental for equipment, subcontractors, fuel for equipment, and anything that you do not take with you for the next project. You can break these down for your budget into separate larger categories if it helps or create a lump sum amount as a cost of sale for your budget.

Subcontractors are one such category that can rapidly increase or decrease depending on the size and skill set that your business has to offer. Perhaps you are deciding to transition towards a full design-build firm of outdoor living spaces. In this case you are likely going to need subcontractors for gas, plumbing, and electrical. If you have not done this type of work before, you will see an increase in this category for this year. Rental equipment is a good cost of sales item to track from year-to-year to decide whether or not it would be a good decision to invest into that piece of equipment rather than continue to rent it.

Though cost of sales items are factored into every project and are not calculated as an overhead expense would be when quoting a project, it is good to get an idea of how much in material costs you will be charged for throughout a season by budgeting for it much like we may budget for anything else. This can be calculated by looking at last year's total cost of sales and adding a certain percentage on top of that to account for the growth that you are estimating for in order to reach your sales goal. This is a starting point to understanding how much money you are going to be spending on these items for that upcoming season.

One great way of reducing cost of sales items is to speak with your suppliers coming into a new season and asking them if they would consider providing you with a discount on supplies because of your previous year's sales with them. This is a good negotiation tactic if you are spending a significant amount of money at one place and are loyal to them over a number of seasons. Alternatively if you have the storage space, you can purchase in bulk to save on costs. However, you still need to account for that space as an overhead expense if you are not already.

It is important to add a markup to the cost of sales items. This is typically an arbitrary number that accounts for the work that you have to do to coordinate and get these items to a job site or if there was ever a warranty issue with items. For example, plants typically have a high markup depending on the failure rate that they may experience. If you plant four bushes and one of those bushes die, you have a 25% failure rate. You want to account for that percentage in your markup along with an additional amount for the labor that it would cost you to replace that plant. This may be less for hardscape materials, but it should nonetheless be accounted for. As you have more experience in business, you will learn the failure rate of these specific items and be able to account for it in your cost of sales markup for each category.

Marking up a subcontractor also allows you to recoup the cost of time that your business allocates to coordination with that subcontractor as well. The markup to rental equipment may be for downtime that you will inevitably experience with that equipment.

Be careful listening to others about what they markup costs of sale items by. They could have a high percentage markup on materials, but a low profit margin or vice versa. Markup on cost of sales is an arbitrary number that could technically be made up in the profit margin on a project.

Profit

Think of profit as a return on investment in your business. You take on a lot of risk as a business owner, something that a salaried position working for someone else would not experience. You should be compensated for that risk and that is your return on investment.

But how much profit is healthy?

You can look at industry benchmarks on this, but to be honest it may not be helpful because so many construction businesses are not making a healthy profit like they should be. You could speak to others on how profitable they are, but are they talking about net profit or gross profit? Are they including their owner's salary in their profit or are they not even paying themselves a salary?

When deciding on a profit percentage, think about your goals that you are creating and aiming towards in your business for the year that you are budgeting for and the years to come. Try pricing a project with your budget as it is prior to adding a profit percentage and compare it to your market. How much lower are you compared to your market? How much can you add on top of your price to get within a reasonable range for where you are in your business?

This is something that you may want to play around with, but as a starting point you should think about where else you could put your money safely to earn a certain percentage with no risk. You could invest in a broad range index fund that covers the market and earn an average return of 8% per year. This takes no skill, no risk, and minimal time to accomplish. It only takes capital. Now how much should you be earning on your business investment each year to make it worthwhile? Twice that percentage? Three times? Eventually you will hit a point where your market will tell you no, but it is an exercise worth thinking about.

Profit is quite simply the money that a business earns after everything has been paid. You can forecast a profit amount and include it in your estimates. You will not truly know the profit that you earn on a project until after that project is completed. For example, maybe you added 10% profit into your estimate but your crew took longer than expected, you fell short on materials and needed to order more, or a piece of equipment that was crucial to the project broke down. That lost amount will

negatively affect your profit. Alternatively, maybe your crew finished ahead of schedule. This will positively affect your profit for that project.

When we are calculating how much profit we want to make on a job, we are talking Net Profit. This is the profit that the business earns after all costs of sales, expenses, labor, and taxes are paid for. This number is not to be confused with what the business owner earns. If the business owner takes home all of the profits that the business makes, then that is their salary and the profit is zero. The business owner's salary is deducted from the revenue of each project much like any salaried employee would be.

Profit is calculated as a percentage amount on top of your total for the project or based on each of the services that your business offers. Your profit can be calculated as a percentage of your total estimate or added into various services that you offer. For example, in our hardscaping business we offer many different services. We do hardscaping, softscaping, landscape lighting, and installation of features like fire and outdoor kitchens. Each of these come with a different percentage of profit. Landscape lighting brings with it the highest percentage of profit for our business and is also why we promote this to others to improve the profit in their business. It is an easy skill to learn, has a high profit percentage, and looks incredible. Maintenance work typically comes with a lower profit margin in comparison to landscape and hardscape installations.

Margin vs Markup

Profit margin is the added amount on top of all of these costs that is the margin you are making in your business. Profit can be used in your business as you see fit. Bonuses for employees based on performance, owner distributions, investing back into the business or all of the above.

This is not a markup. There is a major difference and can cost you money if you do not know the difference between the two. A markup is multiplying by the percentage. For example, $100 x 10% markup = $110 but that is not a 10% margin. That is a 9.09% margin ($10 / $110). That might not seem like a major difference, but when you are doing $1,000,000 in sales that gets to be a big number.

To get margin, you need to divide by the inverse percentage. So if you want a 10% margin, you would subtract 100% - 10% = 90% as the inverse. $100 / 90% = $111.11. With the profit margin being 10% because the profit $11.11 / $111.11 = 10%.

Sales

As discussed throughout this content, setting goals in your business helps to direct where you want to take your business and how you are going to accomplish that. Setting a sales goal will help you determine what decisions need to be made for that year in order to accomplish that sales goal. This will help to direct certain overhead expenses, labor costs, and equipment purchases.

When it comes to setting sales goals for your business, it is important to be realistic and to brainstorm ways in which you can accomplish this goal. Most businesses want to grow, but by how much each year and what are the constraints that are put on growth? Capital is an important constraint which can limit the purchases of equipment that can drive growth. Market trends can limit the amount of demand for your services. Additionally labor can be hard to find and can limit the number of crews you can put onto the road as productive labor.

Consider these variables in your sales goals and think how many weeks of production you have available while also looking at previous year's sales in order to set a sales goal in your budget. If you are increasing your sales goal from the previous year, how are you going to accomplish this?

You could simply add more crews to take on more work. Equipment can be added in order to become more efficient and complete more work in a season. Services that add to the scope of a single project while minimally adding labor time can be upsold on every project in order to increase the price of every project. A year can be extended past the usual time allotted due to winter by using heated tents to complete some work or ground thawing blankets. All of these are various aspects that can be used to increase sales goals from previous years.

Your increase for your sales goal from the previous year's actual sales can help to drive certain aspects of your budget. This was discussed with labor and increasing labor by the amount you plan to increase your sales. There are some nuances to this as you increase crews, you may also be increasing non-productive labor like assistants, designers, or salespeople.

The same percentage can be applied to other expenses such as your marketing budget. In order to increase sales, you need to increase the number of leads coming into your business. That may mean increasing your marketing budget by the same percentage in order to increase the number of leads. This may also differ as you may be investing a lump sum amount into something like a website.

To further this discussion, you should always know your closing rate. How many projects do you close on versus how many leads come into your business. If you get 100 leads and close on 10 of them, you have a closing rate of 10%. Even though you

may not meet 100 of those leads for a consultation, it is important to this process to know the number of leads that come into your business to create a project that you take on.

If you take on 20 projects per year with a 10% closing rate you need to have 200 leads coming into your business. So if you want to increase your sales by 100%, you need 400 leads to come into your business. Once again, there is some nuance to this as discussed previously. This makes an assumption that you are not going to change anything in your services that you offer. If you are also planning to add services to existing projects that do not take up significant labor time, this can reduce the number of leads you need to come in to increase your sales.

All of this will provide you with a company wide budget. Depending on how many divisions you have or how two crews may differ in your business, you may have a company-wide budget and a budget for each of your divisions. The company wide one shows how much money your business needs to make in the season while each divisional budget separates that budget into the various crews.

This can be applied to your sales, as sales budgets can be then allocated to various sales people based on their experience and how much they should be bringing into the business for that year. This is a great way to begin to set goals for your employees and have a bonus structure in place so that they have an incentive to reach those goals. The same thing can be applied to the crews doing the work where they have a timeline and a profit margin that they need to make on that project in order for them to receive a bonus for the project. It allows them to take responsibility for lost time or wasted materials, as the more they are able to be efficient with materials and time on a job site, the more money they will make. This is where job costing during and at the end of a project plays a major role.

Updating the Budget

A budget will help you to set a road map for your business in the year ahead. It will help you set your goals and put a plan in order to achieve those goals. Every cost can be attributed to every quote that is sent out to ensure that you are making the money that you need to remain in business.

If this is your first budget that you have ever created, try pricing a project as you did before and pricing a project with your budget in place. Compare the difference in price. Also, compare it to your market. You can quickly become carried away with your budget and exceed the pricing to which the market suggests. Hiring five employees and purchasing a large piece of equipment for each of them without taking on more work will lead to an increase in price in order to pay for those employees and those pieces of equipment. There is a convergence between cost

based pricing and market based pricing. Budgeting helps you to find that point and to ensure that you are making enough to recoup your costs.

Budgeting also helps you to job cost. This is the process of comparing the actual numbers and the estimated numbers to see what may have gone right or wrong in the estimating process or the build process. Without a budget, you will not know all of your costs on a project. You could compare the labor hours and the materials used, but you would not be able to account for the overhead expenses that go into every project. Those are the hidden expenses that can really put you out of business if you are not thinking about them.

Revisit your budget whenever something changes in your business. If a new employee is added that was not accounted for or if you are planning on hiring an employee. The same thing when you are purchasing a piece of equipment. Ideally, you are planning these purchases and hires prior to creating your budget so that you can be accumulating the money required for that purchase prior to purchasing it otherwise it is coming out of your profit. If you budget for those purchases, you are accumulating the money for those purchases. You can quickly get carried away with this though and say that you are going to purchase more equipment than you require and price yourself out of the market. There is a limit to which you can do this and this depends on what the market suggests for pricing.

If your job costing suggests that you are not accounting for costs or inefficiencies, it is time to revisit your budget to account for those so that quotes will account for them. If something happens in the market to decrease or increase pricing, it is time to revisit your budget. An increase in materials costs or an impending recession will force you to look at your budget and to identify areas that if needed you could cut or remove from your business in order to become more lean. Alternatively, you can identify areas in which you can improve to take on more projects and therefore drive more sales to your business.

Evidently budgeting is a crucial part of operating your business and it is the foundation to the pricing structure of any project-based business. Take your time with this process and try to account for everything that goes into operating your business. There is no such thing as, “this is just the cost of doing business.”