

Global Project Strategy (011) (603) 862-3374

*Special issue
on the effects
of the credit
crisis, oil prices
and inflation on
project
management*

The credit crises assures that few projects approved today will come in on-budget.

Credit Crisis, Oil Prices, and Project Management

When I attended a briefing session at Morgan Stanley and Citigroup 18 months ago, I was assured that the housing bubble would have few repercussions. The economy, they insisted, would not suffer. Guess what? They were wrong. In fact, they were quite wrong. But there's more. I was also assured that oil prices, which at that time were about \$80 per barrel, would retreat to the 50 – 60 dollar range. Wrong again!

So, here we are in the midst of credit crises, spawned by the bursting of the housing bubble, and fed by the unprecedented demand for oil and rising oil prices. But the disease is spreading. For those who have ventured into a grocery store lately, the price of food is up substantially. And in the industrial sector commodities have been on a tear.

As consumers we are hit at the gas pump, at the grocery store, and the action of the Fed in lowering interest rates together with higher commodity prices has raised the specter of inflation.

But what does this mean for project management? How will these events impact the way we plan, manage and control our projects?

As we are all aware, while projects do share some similarities, they are fundamentally quite different. So let's begin with

a few changes that impact all projects.

Two of the most visible factors are budgets and time. Consider the availability of money. Lending institutions have adopted more cautious lending practices; both the retail consumer and commercial borrower now find it more difficult to obtain funding. With tighter money new projects will be tougher to launch and existing projects may find their source of funds dwindling.

In any recession, project funds are scarce. If we do fall into recession ... many economists believe we are already there ... expect funding to be hit hard.

But tight money is not the end of it. The real concern is inflation. Usually the Fed keeps a lid on price increases, but this time their hands have been tied. Rather than respond to the threat of inflation they were forced to focus on an economy that was reeling from a credit and liquidity crises. Their only chance of deflecting a potentially catastrophic spiral into a deep recession was to keep lowering interest rates.

But, as many economists have warned, lower rates may solve the immediate problem but may increase the chances of an inflationary spiral. Indeed

there is lots of evidence to suggest that this has already happened. Even worse, like the 1970s we may be headed for a period lead of stagflation where inflation remains high and growth is stagnant.

Inflationary spirals are one of the worst enemies of project managers because budget approvals are received in advance of spending the money. The larger the project, the farther into the future will be the expenditures. While the easy stages of a project may not suffer, the later stages can be significantly underfunded, and the project managers will find themselves in the difficult position of needing more money.

What this means is that it may be more prudent in this environment to factor in a reasonable inflation factor in the budget or even better to provide two budget scenarios one with a modest inflation of three percent and another with an inflation of six percent or more. At a minimum the consequences of inflation should be mentioned in the budget.

Here's the hard part. Project approvals in many companies are difficult to obtain; project managers are under pressure to keep costs and budgets as low as possible. No one wants to propose an "inflated" budget. (Continued ...)

GM IS Finally Abandoning its Gas Guzzling Projects

The culture at GM kept conservative projects alive while competitors saw the handwriting on the wall and promoted forward looking automotive design projects.

With a few exceptions, notably in the prosperous mid-west farm belt, few people want or can afford the big gas-guzzling monsters that were so profitable for GM. Now, the focus is on fuel economy and drivers prefer a Prius, the hybrid that changed Toyota's image to green.

GM has basically ignored the push toward fuel economy and has been stuck on the belief that its customers still prefer the gas-guzzling V-8 engines or at the very least powerful 6 cylinder engines.

It is only recently that GM created a design group responsible for hybrid or

electric cars. Up to this point design had been spread across many groups with the attendant problem of cross functional coordination. Apparently, it has not worked since GM now lags many of its competitors like Toyota who had a group dedicated to Hybrids in 1995.

Now GM is trying to play catch-up. They finally have a separate group dedicated to hybrids and have moved forward with a controversial electric car called the Volt that will debut in 2010. However, due to their late start and due to the fact that competitors like Toyota have had much more time

to develop fuel-efficient technologies, the Volt will cost 2 ½ times more to manufacture than the Prius.

What does this say about Project Management? There are clearly lots of lessons here, but the one that really stands out is the insular nature of mature bureaucracies and the affect they have on project culture. The GM team headed by Wagoner and Lutz created a conservative project culture that resisted and ignored compelling data that the world had changed. They finally have changed their tune but it took a major crisis to force them out of their comfort zone.

Credit Crisis Continued



Consider the Big Dig in Boston with an initial price tag of 2 billion and a final price of 16 billion. Sure, not all of it was inflation but a good share of it was. Imagine if project management even suggested, at the time of approval, that the cost could double to 4 billion. Chances are that the project, already controversial at 2 billion, would have been shelved.

So, in this environment of high gas prices, a depressed real estate market, and a continuing credit crunch there is not much good news to report for project managers. But there does seem to be a light at the end of the tunnel. In the last four months we have heard relatively little new news about the credit crises. Bank stocks, a reasonable predictor of the crisis,

seem to have bottomed out, and there has been some encouraging economic news. Even the housing crises appears to have moderated.

The Inflation threat however, remains and Project managers have to decide if price increases should be built into their proposals.

91 South Street
Portsmouth, NH 03801
USA

PHONE:
(603) 862-3374

MOBILE:
(603) 767-0480

E-MAIL:
bshore@globalprojectstrategy.
com

We're on the Web!

See us at:

www.globalprojectstrategy.com

Solar Energy Projects

The recent run up in oil prices to \$135 per gallon have suddenly spawned a rush to solar energy. One plumbing contractor in my city told me that he had received a desperate call from a homeowner who wanted to know if solar could save him some money. Next winter's fuel bill to heat his 5,000 square foot home promised to break the bank.

Many are rushing into a solar project without carefully doing their homework. Solar is still costly and may not provide a reasonable payback. Yes. It's fashionable, but is it a good investment?

Others are rushing to trade in their gas guzzling vehicles and favor a more efficient "family sedan" or

hybrid.

But For the most part solar heating systems as well as fuel efficient cars hardly pay for themselves when the cost of the solar installation or the premium paid for a hybrid car are considered.

Too many projects are approved with only a superficial math analysis!

What VISTA's Failure Says About Project Management

The news this month from Microsoft was confirmation of what many had thought for a long time; users were not satisfied with VISTA. Perhaps it was the long wait that kept expectations high. Microsoft had a gap from 2001 when it introduced XP until 2007 when it announced Vista. Users were sure that VISTA would be worth the wait, but the results proved otherwise. Now, Microsoft has announced that VISTA will no longer be bundled in new computers.

Business week said it could be one of the "great mistakes in tech history." Indeed Apple seems to be filling the gap. Even their corporate sales are up!

The complaints about VISTA are long: it has few new features that users want; has frustrating glitches; forces companies to train users; and also requires new and faster computers.

While we may never find out what happened during the VISTA project what is apparent is that the project failed.

How it did fail is a matter for speculation but communication failure is certainly one very likely possibility. Let's assume that effective market analysis was conducted and that the final design of the product promised to compete well in the marketplace. But over the life cycle of the project,

Microsoft apparently did not solicit feedback from potential customers because an alarming 1/3 of current users are dissatisfied with the product. How could they have missed by such a large margin? One explanation is that they wanted to keep the new features secret and out of the hands of competitors.

How is Vista doing in Europe. I was there last week and when I mentioned Vista almost everyone in the room laughed.

Lesson Learned:

Keeping customers out of the project loop can add to project risk.