SURVIVING THE MAKE OR BREAK MOMENTS

EFCG’s Annual CEO Conference in New York city brings together business leaders from across the professional and technical services sector to share industry insights and discuss the hot topics of the day including how to prepare for a downturn, M&A trends, technology as a differentiator, globalisation vs retrenchment and much more... Environment Analyst presents a round up of the latest meeting.
Industry overview

October 2019 marked the 39th Annual EFCG CEO Conference in New York City, hosted by sector specialist financial and advisory group EFCG. It brought together more than 200 CEOs of the leading firms across the architecture, engineering and construction (A/E/C) - also encompassing environmental consulting - sector to debate the key trends, threats, and opportunities facing their businesses.

Topics include timely issues such as the talent dilemma, diversity & inclusion, and how to prepare for a potential recession, complementing core themes based on EFCG’s industry metrics and performance data and analysis, sourced from the firm’s 30-year proprietary database focused on the A/E/C industry. One of the major draws of the day was the CEO panel sharing experiences of their ‘make-or-break’ moments.

First up EFCG managing partner Rebecca Zolnossy highlighted the key results from EFCG’s 2019 CEO Survey and what they reveal about the wider industry’s performance metrics:

- **Profitability:** 2018 median profitability (EBIT/net revenues) came in at 11.6%, just below previous estimates, while median profitability for 2019 is expected to be around last year’s projections at 13.1%. 2020 profitability is also projected to remain strong. “CEOs report they expect profitability to continue to improve, which is likely driven by a greater focus on profit and efficiency across the industry,” Zolnossy says.

- **Growth:** Actual internal net revenue growth for 2018 came in at 8%, with the strongest revenue growth performance observed in larger firms. “For 2019 and 2020, forecasts of growth to plateau at 8%, whereas we expect a small decline.” Over the next decade, industry continues to grow, and the dataset suggests that even in a downturn, the median growth remains above 7%.

This makes the industry resilient. Notably, in the last five years, we have seen the highest growth rates in the economic downturn of 2008.
identify what makes marketing initiatives more or less successful in closing deals. Although BD/marketing investments should be driving proposal hit rates, EFCG notes that it does not observe a correlation between these metrics from the last year’s data, which means that “there exist multiple opportunities to increase the effectiveness of BD/marketing investments”.

“BD/marketing leadership teams should consider whether and how the BD/marketing ROI is measured and evaluate brand awareness and perception among clients and prospective employees.” Furthermore, it is also important to focus BD/marketing investments based on how the firm gets work from clients (e.g. bid vs. sole-source), evaluate the types of sales structures used, and evaluate their effectiveness in facilitating new work.

Risk: in today’s highly unpredictable political and economic environment, knowing more about an a/e/c firm’s risk profile across a wide set of metrics enables better decision-making with regard to where the firm is willing to take more or less risk. For this reason, EFCG has developed its “Risk Index”, based on a firm’s profile across the following metrics: leverage, profitability, use of alternative project delivery, client concentration, share/buy-backs, accuracy of budgeting/forecasting, working capital management, and diversification.

This year, it found that about 90% of a/e/c firms assume construction risk, while around 90% of those do design/build (D/B), and 40% do construction management or general contracting (CM/GC). About 5%-23% of revenues are generated from construction, which raises the issue of how can a/e/c firms provide such services without taking excess risk.

In terms of client concentration, EFCG observes that smaller firms generally have greater concentrations, with around 50% of the revenues generated from their top 5 clients. This is riskier, it suggests, as a firm may be overly dependent on continuing work with a few key clients.

On budgeting, actual results need to match projections in budgeting, which impacts profit margins, ability to sustain a level of activity, and cash flow. Naturally, the greater the gap between projections, the more challenging it is to achieve the desired operating margins.

EFCG suggests that talent is likely to remain among the most significant challenges for the foreseeable future. Even if a firm is good at talent acquisition, if turnover is high, there will always be a talent shortage. Marketing and business development are meaningful enablers, but not always spent effectively. Companies should strive to consistently monitor marketing and business development spend to ensure these functions are benefitting the overall strategy and success of your firm.

M&A success rate, culture and valuation trends

2020 expectations

Overall, 2019 seemed to be a strong year across the industry, and 2020 projections show that the industry is not expected to slow down. However, even if a recession does not occur, knowing your firm’s full risk profile is the first step to ensure that you can withstand challenges and diversities, and emerge as winners in the next cycle.

Based on EFCG’s 2019 CEO Survey results, M&A activity continued at a strong pace in 2019. Furthermore, projections of 2020 are more conservative than in recent years, which could be due to increased economic uncertainty and particular interest in acquiring a firm and waterfront projects.
Technology as a differentiator

It comes as no surprise that senior business leaders continue to highlight technology as a differentiator as being one of the most important trends. At EFCG’s 2019 Technology Conference, 88% of firms reported technology as a differentiator to win or defend their market share, and they use it as a differentiator by 92%.

According to its 2019 report, EFCG states that the annual growth rate in innovation, innovation, innovation, innovation, innovation, and technology-driven net revenue of FTEs is driven by the rapid adoption of new technologies and advancements in technology.
Diversity dismay and the talent lifecycle

The most recent EFCS CEO Surveys indicate that the a/e/c industry has not made significant progress on diversity over the last decade. Currently, women remain less than 30% of all employees and minorities are slightly over 15%. However, there are emerging signs that diversity numbers may be improving.

CEOs believe the greatest challenge to attracting and retaining diverse talent occurs during the recruitment phase. Diversity worsens at more senior levels, with just 15% female and 6% minorities, which likely impacts recruitment success.

EFCS managing partner Julie Hasiba and Kelly Reed, Lockton managing director, presented and moderated a panel discussion on talent. The session explored the different stages of the “talent lifecycle” from talent acquisition to alumni relations. Insights from EFCS’s annual CFO and CHRO Conferences were brought in to express some of the common themes and perspectives shared by other critical senior leadership in the industry.

This year, CEOs rated talent as the top concern in the a/e/c industry. Furthermore, research and results from EFCS’s 2019 CEO, CFO, and CHRO survey data indicate a number of specific concerns, including talent war & budget constraints, employee retention, skills gap and role vacancies, and lack of diversity.

All these issues are significant as they can impact firm costs, vacancies, culture, and adaptability, suggests EFCS. “For instance, high voluntary turnover in a competitive market, along with a constantly increasing skills gap and lack of diversity and budget result in high turnover costs, challenges in filling vacant positions and company challenge, and other critical senior leadership in the industry.”

Yet, despite these challenges, the tools and data to generate diversity and inclusion can evaluate where their organizational talent and company culture strategies are. EFCS has developed a framework to be used during an employee lifecycle where it can identify who are high performers as new employees and ensure they are engaged and aligned with the company’s goals.

Alumni Relations
Maintaining connections with former employees to create “ambassadors” and encourage boomerang

Transition Planning
Planning for employees’ departure or movement to a new role (incl. handing off responsibilities)

Career Pathing
Communicating with employees to identify future role(s) in the company and aligning goals with these opportunities.

Talent Retention
Keeping employees who add assets to the company

Value Creation
Contribution of the company.
Global perspectives

EPCG’s Julie Hasiba and International Director Andreas Georgoulas moderated an International Forum at the NYC meeting. Discussion topics included the impact of the increasingly global nature of this industry, how policy impacts business across geographies, and how seeing your firm as “global” versus “international” changes its overall strategy, business partnerships, and even ethical standards.

The panel provided a thorough overview of the trends, challenges and opportunities in different parts of the world. The Asian market was noted as stable, except for China which seems to be slowing down. On the other hand, outside of a select few countries, the Latin America and Africa markets are not strong. Project activity in Africa has decreased, while in Latin America firms are focusing on helping mining and industrial project operators to avoid accidents. Notably, recent dam disasters have made insurance carriers hesitant to provide professional indemnity, and insurance premiums seem to be going up by double digits every year.

The European market is seen as very strong.

Sustainability trends

Starting with global sustainability trends, demand comes generally in two streams: (1) helping clients deal with liabilities, and (2) helping clients enhance value.

Strategies are focused on sustainability and social responsibility. Sustainability can bring in new growth opportunities, but impacts can be significant. The right sustainability decisions can be beneficial and can beat competitors.

Another major trend is water management, which is a critical issue in many parts of the world.
marketing strategy and value proposition to recruit the right talent.

Another significant aspect is the need to train and develop people so they can be international managers. The ideal profile would be someone who has been exposed to different types of cultures, clients and countries, and can adapt and lead an international team with an international client.

Global expansion

The globalization discussion concluded with the aspect of expanding in new countries, and whether organic or inorganic growth strategies are better. Acquisitions are preferred if the firm is in a hurry, as it enables you to get the top talent in the area. Yet, in the case of a small, external player, it will not work well in a new country. The firm would most likely be hiring a second-choice employee base and will not be able to attract a strong CEO.

Firms with global operations can consider different ways to grow abroad, either by setting up a local company and investing over the long term, or by following a specific client for a short time and a given project. A panelist from an architecture firm stated that they don’t consider opening offices abroad because that gives them the advantage of being considered the unique expertise that has to come from overseas when being pinned against an “everyday” local firm.

CEO tips for surviving make-or-break moments

EFCO’s Jessica Barclay moderated the CEO challenges and responses session. Panelists discussed some of the key challenges they’ve faced in their CEO role, how they overcame them, and shared with the conference participants the biggest lessons learned.

Summarizing the panel’s shared wisdom, the key pieces of advice are:

- Keryn James, CEO, ERM: “Know what your gifts are and what they are not.”
- Hisham Mahmoud, CEO, Geidor: “Do not do things just because it is the way it has always been done. Look at how things should be done.”
- Tom O’Grady, president, HNTB: “Make the right decision for the firm you are working for, not just your individual unit or group.”
- Dan Buttrick, CEO, TetraTech: “Don’t be afraid to make the hard decisions.”

We did not try. We wanted.
Learning from historic trends in preparing for a downturn

EFCS’s Georgoulis presented an analysis on historic trends in the a/e/c industry and how to best prepare for what lies ahead. A panel of CEOs then shared how their firms were successful through past recessions to see how they put theory into practice.

The session began with a presentation of the EFCS analysis on the past ‘great recession’. From a pool of over 250 firms, the study identified 62 firms that had consistently provided financial data from 2005 to 2018. The firms were divided into four categories based on 2004-2018 net revenue growth and EBIT margin performance (Figure 1).

Then the financial data of the 62 firms were evaluated to ascertain why certain firms performed better and the critical indicators that allowed them to do so. Overdiversified, efficient, and productive firms had a competitive advantage during the downturn. Most of the time, they exited even better.

Top-performing firms should diversify selectively to source services, and regions, to allow impacts. Firms with exposure found an advantage in different parts of the exit a market cycle.

Shelle Gustafson continued with an overview of how Jacobs endeavors to be an employer of choice and considers employees as partners in achieving success, stating that “Culture isn’t owned by HR. Culture is owned by everyone.”

Gustafson described how Jacobs considers the relationship between business challenges and HR priorities to align capabilities, business change, and develop business-aligned talent strategies to hire right talent and drive a culture.

She concluded with sharing the diversity at Jacobs in terms of commitment and engagement for employees, which allows for an inclusive firm able to attract talent and leaders.

In turn, such diversity provides a competitive advantage in the market.
industries have (e.g., manufacturing), and firms first of all buy key people through acquisitions. As such, a firm should not look for deals or clearance pricing but focus on acquiring firms with a strong balance sheet and cash flow.

The discussion continued around preparing a plan to deal with a potential recession. Each firm needs to understand their business mix, but many don’t understand where and how they make money. All firms need a plan to look at what they can perform well without and avoid large investments. Firms should monitor key performance metrics very closely and establish performance thresholds, so if a metric drops below the threshold they can make decisions very quickly and make the necessary adjustments. Then, they can start diversifying in their markets and get smarter on their cost base. Another crucial aspect is getting comfortable on doing more with less people, which means less spending and expenses.

The best clients should be targeted to ensure that most work is done for clients that are stronger financially, and the clients that are very strong financially should be avoided. The need to know who the firm’s high profit clients are and the office locations that support the profit the firm is looking for. A crucial aspect is to be able to plan for a recession hits, and forecast the financials so if such indicators..

The discussion identified a number of mistakes made in the past as a recession hits. Historically...