SAMPLE REPORT

Environment Analyst was delighted to be invited to the inaugural CEO Summit hosted by AEC Advisors LLC, M&A, valuation and corporate finance advisory specialist focused on the architecture, engineering and consulting industry, which was held in New York last month. The three-day event attracted 260 CEOs from firms operating in the AEC sector - many with an environmental consultancy offering - across the US and globally, including industry leaders based in North America, Europe, Middle East and Australia.

Environment Analyst explores the key themes debated at the recent professional services industry CEO Summit in New York, highlighting the most relevant takeaways for environmental consulting leaders - whether operating as specialists or embedded in broader scope AEC firms. Including if stakeholder value and a broader responsibility to society can influence environmental outcomes.

Strategic Imperatives From Diversity To Digitalisation Dominate AEC CEO Summit
KPIs - are you on a virtuous or vicious cycle?

Kicking off a packed agenda, AEC president Andrea Avellini gave a comprehensive overview of the findings from the AEC Advisors’ 2019 KPI survey, which collates and analyses the results from 230 firms (representing combined revenues of $130bn) on a range of metrics – indicating the size, structure and state of health of the wider sector in which environmental consultancy is one facet.

Whilst still a highly fragmented industry, with an estimated 2,000-3,000 firms (of 20 staff or more) operating in this space in North America alone, the revenues are heavily concentrated in the largest players, with the top 18 firms representing around 70% of overall combined revenues from the 230-strong survey pool covered by AEC’s benchmark survey.

A core and repeated theme from the findings presented by Avellini was the differential in the KPIs of the most profitable firms vs the least profitable, with the former displaying faster growth, 4x greater profitability, higher bonuses/compensation and lower turnover, and hence their tracks on either a virtuous or vicious cycle. Regardless the KPI, he suggests firms should strive for the top quartile.

Summarising the survey findings Avellini made five core observations which set the foundations for the subsequent discussions on the respective panel sessions throughout the event, namely:

- **Prepare for a downturn:** Survey responses predict slower growth next year compared to this year, which jars with the usual optimism seen in this industry’s growth forecasts. Given the past recession-free decade in the US, expectations of slowing economies in key regions and increased geo-political risk globally, Avellini feels there are sure warning signs of what’s inevitably to come. He reminds delegates that the AEC industry typically goes into a recession, due to the project pipeline nature of many of its clients which acts as a natural buffer, delaying the impact of a downturn. 2020 is the time to seek operational efficiencies, whilst there is still work to be done.

- **KPI benchmarking:** Those KPIs you want to improve, or build on a powerful model of improvement, is more work than most firms are prepared to do. KPIs that matter are more work than most firms are prepared to do.

- **M&A strategy:** An M&A strategy is crucial, regardless if you’re buying, selling or neither. If you want to grow faster, acquisition is a good option, particularly now given the ease of raising capital (including from PE). For owners who aren’t able to transition ownership internally, it can be a great exit strategy, and currently conditions favour sellers over buyers.

- **Diversity & digitisation:** The two most important success factors over the next ten years will be diversity and technology/digitisation, predicts Avellini. With too many firms still fighting for “white males”, solving the “diversity puzzle” will be critical to attracting and retaining top talent.

- **CEO leadership:** The most important success factor in this industry? None more so than CEO effective leadership for AECs. The other factors will mean very little if professional service assets are perceived as merely “the task forces” which deliver the outputs for the CEO. The problem is that CEOs often place too much focus on the outputs, and not enough on the inputs which drive performance.

The challenge is that organisations today, yet again, are missing the link between inputs and outputs, becoming their own worst enemy. The solution is obvious, but how many CEOs are truly willing to do the work? The KPI survey results provide the evidence that a virtuous cycle is possible if the inputs are scrutinised, managed and guided with a relentless focus, making them a beacon of success.
The closer the acquirer and acquror in size, the greater the struggle...
Since going public back in 1995 it has completed roughly 150 M&As, with the most significant deal to date bringing on board 7,000-strong MWH Global three years ago (EA.11 May 16).

Moriszak, who personally has been involved in around 100 of these, believes simply that in any transaction strategic fit goes hand in hand with cultural fit. He stressed the importance of spending time up front with potential acquisition targets pre-merger, prompting Avelin to ask how often Stantec walks away from a transaction at this stage. "Very rarely," he concedes.

"[In M&A] you should not be led by your CFO"

It's a fine line to tread, based on instinct in Moriszak's experience. "You make a judgement upfront." As Avelin concluded, you don't want to get a reputation for walking away during the due diligence process, nor do you want to get sucked into a bad deal.

But once you've identified your target, established your compatibility, paid the (right) price, acquiring firms are still not out of the proverbial woods. All too often mergers, whether bolt-on or transformational, are followed by a stream of staff - the 'assets' you have just 'bought' with the core experience and client contacts you sought - making for the door, in a people-based business, that can be catastrophic.

Jay Wolverton, founder and transportation and civil engineer, Wolverton, which was acquired by fellow consulting engineer CH2M, communicating the deal, for supporting it, is on employees on board. On a more positive note, giving key members of the acquired firm "meaningful roles" in the new entity, "Integration sounds like a bureaucratic process but it can be a living breathing thing," Goldfarb stated.

- Establishing an 'employee council' is a voice post-merger, according to Avelin.
- CEO Ernesto Aguilar (whose recent exits have included Design South, AndersonPenna Partners, and ECi Consultants, and then Engineering, a Florida in 2017).
- Managing an autonomy at a staff level leads to new roles.

"Total Shoa, Der Group"
M&A in bearish conditions

Based on recent economic history, recession is long overdue in the US, and Avelino asked the panel if forecasts of a downturn were influencing their M&A strategies.

Interestingly, both Dar’s Shair and Cardno’s Ball were in agreement that recessionary conditions and market cyclicality can represent opportunity.

Proof of this perhaps for the former was Dar’s unsolicited A$2.9bn (US$2.2bn) takeover bid for WorleyParsons (as it was then) at the end of 2016 with the Australian firm – and its stock price – struggling following the collapse of global resource markets. Whilst the takeover ultimately failed it did secure Dar a “strategic stake” in the Australian player (EA 28-Feb-17).

Ball’s own Australian firm Cardno also felt the full heat of the resource downturn, ultimately leading to the entry of PE Crescent Capital as a majority shareholder (EA 12-Nov-19). But having come out of that tunnel stronger and wiser (EA 03-Apr-19), he explained that buying a company at the bottom of the cycle can be advantageous from a risk perspective: “Owners get scared when they see their markets going down but as a bigger, more diversified group, Cardno is well able to navigate those downturns, if we can make the numbers work on a depressed margin basis, it’s better for us.”

Divesting as a strategy

Hand in hand with M&A comes divestiture as part of the strategic review process. Certainly we have seen some major announcements in recent months from some of the market leaders involving radical overhauls of their operations: again, we come to Jacobs’ decision to sell its ECR arm enabling it to “expand in high growth segments” including water and energy and move away from “narrow, low margin markets”; meanwhile AECOM revealed that it is looking to sell its geotechnical management service arm.

But divestments do not have to be seen as negative companies. Indeed, divestment can help make a business a more focused entity.

Along with a number of other companies, AECOM has been embarking on a review of its operations. It recently divested its AutoNOMY business unit to Nauto for an undisclosed amount, following an “aggressive programme of investment” in the technology as well as the development of a range of applications.”
Arcadis itself, Oosterveer outlined, has three clear horizons in terms of its own digital transformation:

- **Today**: 100% BIM (and Oosterveer acknowledges that the industry has been slow to introduce BIM as standard to all its activities)
- **Tomorrow**: the adoption of pre-existing digital technologies
- **Future**: the co-development with selected partners of new technologies under amongst others the TechStars programme (EA 12-June-18) and the creation of new business models

And Cardno’s Bell is in no doubt that technology, data management and digitisation will “fundamentally change this business over the next five years”. But like Arcadis, he admits that Cardno’s Ball is in its own journey, and currently the emphasis is on identifying vendors, who are “way ahead of the AEC industry presently”, and buying in the expertise from them rather than outright acquisition.

It’s a warning that perhaps AECOM has learnt the hard way, with that firm’s design & consulting arm president for the Americas Steve Morissi admitting that their enthusiasm for all things digital went “a bit wild west” at one point before they reined it in and identified a handful of priority areas. His comments chime with those made to Environment Analyst earlier this year by his colleagues in the UK (EA 14-May-15). That said, Morissi is quite clear that technology represents an opportunity for AECOM.

And a “strategic imperative”, and its commitment to technical excellence to best serve its clients.

“We recognise that innovation, technological advancement in areas such as machine learning, artificial intelligence, the use of drones for example, is revolutionising our industry. At Golder, we have a program to support us in this. It’s critical to recognize that companies do not have the means to develop comprehensive new programs and will need to work with others in the industry – whether universities, partners, vendors, etc.”

Furthermore, James Miner, CIO/Chief Technology Officer at AESCo, believes that technology and digitisation are part of the solution, not the problem:

![James Miner](image.png)

*“Technology should be seen as a tool and not the answer.”*

A five-year timescale is echoed by Dar’s Shair too. But whilst technology has, and will continue to change this industry, we shouldn’t be fearful of it. “No technology will ever be able to design a smart city,” he argued.

“But just because you can, doesn’t mean you should,” warns James Miner, CIO of interdisciplinary planning and design firm Sasaki. “You have to be sure the technology works for you,” he added. “Every project is unique and the technology must work for the client. You need to know what you need to try new things all the time, and lead the leading edge of the digital revolution.”

“I also think technology is a tool and not the answer, and it must work for the people around us. We all have a role to craft and shape the future of our planet and the planet we live on.”

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Shareholder vs stakeholder value

In fact, the issue of ESG is something that was discussed in detail under the wider umbrella of 'engineering stakeholder value', underlining a growing emphasis on stakeholder value rather than shareholder value than perhaps has been the norm to date.

Here there was consistency, as Avedis noted, across the panellists. *Anser Advisory* CEO Bryan Carnuthers summarised the rub of the issue, suggesting the professional services sector should automatically be looking at stakeholder value over shareholder value because the one leads to the other: “Customers, employees and communities are intrinsically woven into what we do; if you get those things right it will automatically lead to profitability.”

Tetra Tech CEO Dan Batrack is perhaps better placed than most to be able to comment on the shift in boardrooms towards stakeholder value, having spent the past 15 years (of a total 39 years) as CEO of his firm. [In fact, underlining the enviable stability of that firm, he is just the third CEO since the firm was founded in 1966.] But despite being publicly listed, Batrack is quick to assert that no board-level decision has ever been made solely for shareholders, nor has consideration of its share price ever been the only factor influencing its strategy (which is to offer technical consulting excellence, notably in the water sector).

So perhaps a stakeholder perspective is already well entrenched in this firm. (Whether it is or isn’t, that’s not to say that the management hasn’t made some mistakes along the way, he concedes, prompting for example a recent decision to exit certain fixed-price remediation and construction management activities and restructure accordingly [EA 26-Nov-14].)

Looking ahead, as previously noted, recession is on the cards for the US, and indeed globally. Panellists were sanguine about an impending downturn but simultaneously taking all necessary preparation of the inevitable.

Darkening skies are also predicted by Mahmoud, and he cites: “Never let a good crisis go to waste.”

And finally, with a discussion about the seniority of discussions with stakeholders.

Partnership of Water Corporation

...
D&I: requires improvement

Perhaps another way to stand out in a traditionally white male-dominated industry is a demonstrable approach in corporate strategy to diversity and inclusion. AEC Advisors’ Awelini did not hold back by suggesting that diversity of the AEC industry against others is “a sad story” and its gender diversity he referred to as “atrocious”. Underlining this assessment, it did not go unnoticed that of the 260 delegates attending the event, just 10% were female, and the representation from other minority groups equally woeful. White males (of an age) were in abundance...

That said, Awelini recognises the fact that whilst most firms do want to boost their gender and racial diversity there are simply not enough women and minorities graduating out of the AEC’s education pools. But that aside, the findings from AEC’s own survey which created indices for gender and racial diversity indicate that firms with greater gender diversity enjoy lower staff turnover, whilst those with the least gender diversity suffer lower growth and profitability.

The findings also suggest that increased diversity in either gender or racial terms tends to foster the other, prompting Awelini to propose increased benchmarking in these areas industry-wide, with the purpose of praising or indeed shaming firms into improving.

Whilst praising or shaming may be a more radical suggestion for the conference’s predominantly North American audience, it’s something that larger European operating firms (typically with around 250 staff or more) have already had to embrace in the past couple of years. And beyond Europe, some firms in this sector are already taking heed even before being compelled by legislation, as in the case of Carine (EA 3-Jun-19) and Jacobis (EA 11-Dec-18).

Yet in the UK, two years of mandatory gender pay gap report filings show little progress year-on-year nationally despite best intentions; and worse, scrutinising the performance of the leading two dozen or so firms in the environmental consulting sector specifically was a depressing exercise, with the sector comparing pretty unfavourably to national averages (EA 17-Jun-19).

The diversity scene was set powerfully by former Mastercard CFO (and recent appointment to Golder’s board as an independent executive director) Denise Florido who has provided insight into some of the issues she has faced as a woman during her long career. “The comfort of feeling that we have to crack,” she said ultimately an industry-wide, comment from the CEO level down at McKinsey that...
Environmental consultancy under the AEC umbrella

In this comprehensive and highly informative event hosted by AEC Advisors, it’s not surprising that so many themes covered are just as relevant when drilling down to the environmental consulting specialism in which Environment Analyst is focused.

Issues such as diversity, digitalisation and consolidation etc are equally taxing the brains of many environmental consulting firm CEOs as those in the broader AEC field, and hence were also key topics at Environment Analyst’s own annual Business Summit, held earlier in the summer in London (EA 26-June-19).

But there were two areas where the discussions of our respective events differed.

Firstly, the one issue that didn’t feature prominently amongst the discussions in New York was the need for increased environmental and sustainability leadership at a broader level, especially within the professional services sector, particularly with climate change and sustainability never higher on the public agenda than they are currently (although there was a flavour of it around the discussion of the rising prominence of ESG in the boardroom).

But in contrast - and admittedly not surprisingly given the specialism of our own audience - our own event opened with RPS chief executive officer for consulting (UK & Ireland) John Chubb outlining the urgent need for leadership in environmental consultancy to help organisations address the climate emergency; Chubb’s message to his sector peers was simple: ‘Extinction or Rebellion’? The call to action for a sector-wide collaborative approach was one echoed by many of the other speakers at the Environment Analyst Business Summit (EA 26-Jun-19).

And perhaps given this dawning realisation, the second key difference, when considering environmental consultancy specifically, was a significantly more optimistic outlook for the sector’s prospects in the near future. Positive expectations were reinforced by the findings of Environment Analyst’s 2019 Global Trends report for the EC sector which predicted an average improving profit margins, albeit a moderate overall uptick in staff in five years and a strong uplift in prospects (EA 01-Oct-19).

It appears that, even as businesses shuffle the cards and a shake-up continues generally, and not just days after the conference, environmentally-conscious businesses are conferring on how to achieve this.