COMPANIES

E&C Firms Enjoy Good Times But Sound Alarms on Future

Engineering and construction firms seem to be enjoying good times that have raised profits, stock prices and company valuations, but they are still dogged by employee turnover, size and ownership transition issues. And the impact of Hurricane Katrina, changing markets and growing project risk could add to future uncertainties, according to some industry CEOs.

The trends were underscored by CEO speakers and survey data at an Oct. 20 industry CEO conference in New York City, sponsored by EFCG Inc., a New York City-based management consultant. The 187 E&C firms surveyed expected their revenue to grow 10% on average by year end, up from 7% in 2004. Companies were a little too optimistic about profitability for 2005 in the same survey last year, predicting an 11.3% average margin. This year's survey estimates only a 9.8% average profit for the year.

Even so, Wall Street and other investors seem to be scrutinizing the industry's numbers like never before, said Paul Zofnass, EFCG president. While all publicly traded firms on the Standard & Poor's index rose just 4.4% in the last year, EFCG's index of 14 public E&C firms' stock rose 43% in that same time period and 78% if the previous year also is included. That trend also has affected private firms. "Valuations are going through the roof," said Zofnass.

That is great news for company owners looking to cash in their shares, but Zofnass cautioned that overvaluation could affect employee stock ownership plans. Equity investors may provide a short-term capital boost but they can alter E&C firms' culture and management style, he said.

"The valuations are not sustainable," said Joe Zuback, senior vice president of U.S. Filter, Palm Desert, Calif. "They will be coming down."

Alarm Bells

Other CEOs sounded other alarms. Ralph Peterson, CEO of CH2M Hill Cos., Denver, said the firm's experience as a Hurricane Katrina response contractor, highlighted the need for firms to "better manage volatility and build up inventories."

Len Rodman, CEO of Black & Veatch, Kansas City, cautioned about the risks of E&C firms growing too large. Added John Dionisio, CEO of AECOM, Los Angeles, "No matter how many mergers and acquisitions you do, clients are not going to be willing to pay you more."

EFCG said that the number of CEOs listing "personnel" as their key concern doubled in 2005, while 65 of the 187 chiefs cited ownership transition as a "big issue." ■

By Debra K. Rubin

HOW FIRMS ARE FARING

Performance metrics for 95 engineers and contractors with revenue of $25 million to over $1 billion*

METRIC	%
A Loss Year (in last 5 years)	0.7
Growth Down Year (in last 5 years)	15.0
Median Profit Margin (5-year average)	8.7
Median Growth Rate (5-year average)	7.4
Firms in same profit range at least 4 out of 5 years	26.0
Firms in same revenue-growth range at least 4 out of 5 years	12.0

*OF FIRMS REPORTING PERFORMANCE FIGURES EACH YEAR FOR 2001-2005

SOURCE: EFCG INC.