

How to Survive a Recession

Prospering in Cyclical Markets

Dr. Tom Schleifer

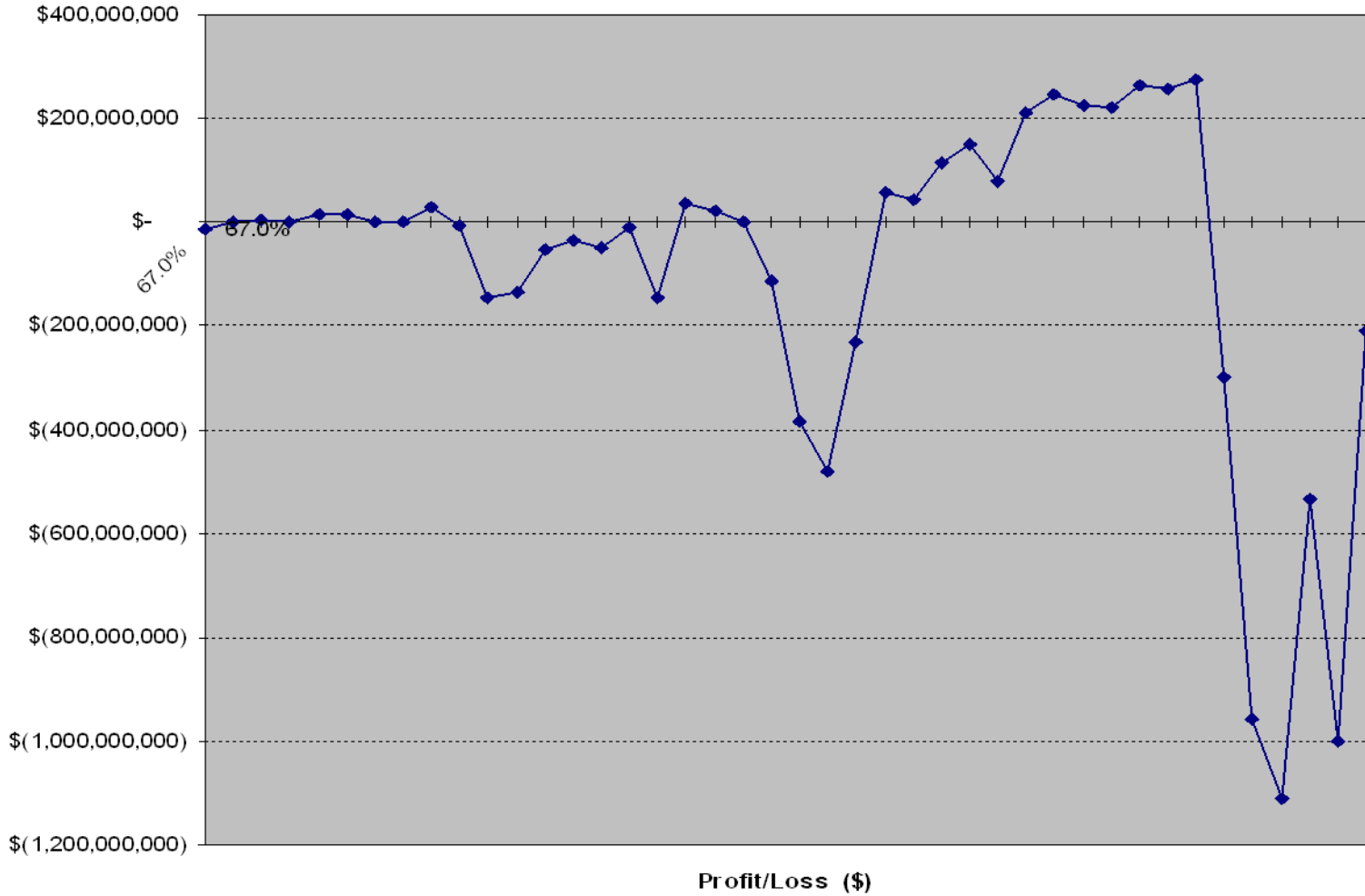
Alliance for Construction Excellence

Del E. Webb School of Construction

Arizona State University

Surety Losses '64 - '04

Surety Results '64 - '05



An Age of Turmoil

After 8 decades of growth to 156 Fortune 500
Bear Sterns disappeared over a weekend

City Bank founded Napoleon, reports huge
losses from sudden and severe deterioration
in sub-prime market

54 Fortune500 post losses of \$115 Billion '07

An Age of Turmoil

- **US Government debt rating may be downgraded**
- **Weakening dollar**
 - Leads to higher prices for imported goods
 - Put pressure on Fed to raise interest rates
 - Drives up the price of oil which triggers higher prices everywhere

Your Company's Growth

- **Being Around For Years And Being a Large Organization May Not be an Asset**
- **Because Somewhere Out There Is a Bullet With Your Company's Name On It**

Jim Collins

- “Companies do not fail because of what the world does to them or because of how the world changes around them.
- They fall first and foremost because of what they do to themselves

Economic Tides and Trends

- Change is a constant, not necessarily fun
- Miss an industry shift, may never catch up
- To stay ahead, need to forecast the market
- Understand construction economics
- Being around years may not be an asset

Agenda

- Timing of Recovery
- Review Elements of Failure
- Tracking your Company's Growth
- Four elements of Profit Potential
- Stages of Growth

Construction Business

Success does not imply future
success

S L I M Margins

L A T E information

Extremely Credit Centered

Timing of Recovery

- Construction is a lag industry
- Recovers 12 to 18 months after general Economic Recovery

Timing of Margin Recovery

- Margin recovery lags construction recovery an additional 12 to 18 months
- Until return to 2007 volumes, appetites will not be satisfied driving aggressive bidding

US Construction Spending

Actual	Actual		Estimated			
2007	2008	2009	2010	2011	2012	2013
150,688	1,072,132	997,740	947,525	994,799	1,065,661	145,842
Change Yr	-6.8%	-6.9%	-5.0%	5.0%	7.1%	7.5%

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Yr on Yr	-6.8%	-6.9%	-5.0%	5.0%	7.1%	7.5%
Yr base	-6.8%	-13.3%	-17.7%	-13.5%	-7.4%	-0.5%

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base	-6.8%	-13.3%	-17.7%	-13.5%	-7.4%	-0.5%
base	93%	87%	82%	86%	93%	100%
2007	2008	2009	2010	2011	2012	2013

Stimulus Money

US Construction Spending

2009	2010	2011	2011	2013
997,740	947,525	994,799	1,065,661	1,145,842

Stimulus Funds

44,274	41,939	16,593	6,295	4,715
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Percent of Stimulus

2.4%	4.4%	1.7%	0.6%	0.4%
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2009	2010	2011	2011	2013
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Impact of Reduction Sales

Co with 4% OH and 2% Profit can reduce 32%

Co with 4% OH and 1% Profit can reduce 20%

Competitive Pressure Causes Aggressive Bidding

Break-even work

Co with 4% OH and 0% Profit can reduce 0%

Enters losses at first dollar of reduction

Common Elements of Failure

- Change in size of project
- Change in geographic area
- Change in type of work
- Change in key personnel
- Change in managerial maturity

Keys to Success

- Understanding the market
- Anticipating industry shifts
- Rigorous Planning
- Continuous improvement
- Successful companies are totally focused on getting better

To Stay Ahead You Need To:

- **Forecast Your market**

- **AND**

- **Understand The Laws Of
Economics**

Four Elements of Profit Potential

- **1. Fit--With Reference to the Market**
- **2. Flexibility with Reference to Technology**
- **3. Stability in a Declining Market**
- **4. Return on Investment**

INTERNAL FORCES

- FAMILY
- TIME ALLOCATION
- OWNER'S ABILITY ...
STRENGTHS/WEAKNESSES
- FINANCIAL RESOURCES

EXTERNAL FORCES

- MARKETPLACE
- COMPETITION
- LABOR
- CREDIT AVAILABILITY
- TECHNOLOGIES
- GOVERNMENT REGULATIONS

DYNAMICS – CLOSELY HELD BUSINESS

- **OWNER'S ABILITY TO DO**
- **CASH**
- **MATCH BUSINESS AND PERSONAL GOALS**
- **PEOPLE—QUALITY AND DIVERSITY**
- **STRATEGIS PLANNING**
- **SYSTEMS AND CONTROLS**
- **OWNER'S ABILITY TO DELEGATE**

Stages of Growth

- 1. START UP**
- 2. SURVIVAL**
- 3. SUCCESS**
- 4. GROWTH**
- 5. MATURITY**

STARTUP SURVIVAL SUCCESS GROWTH MATURITY

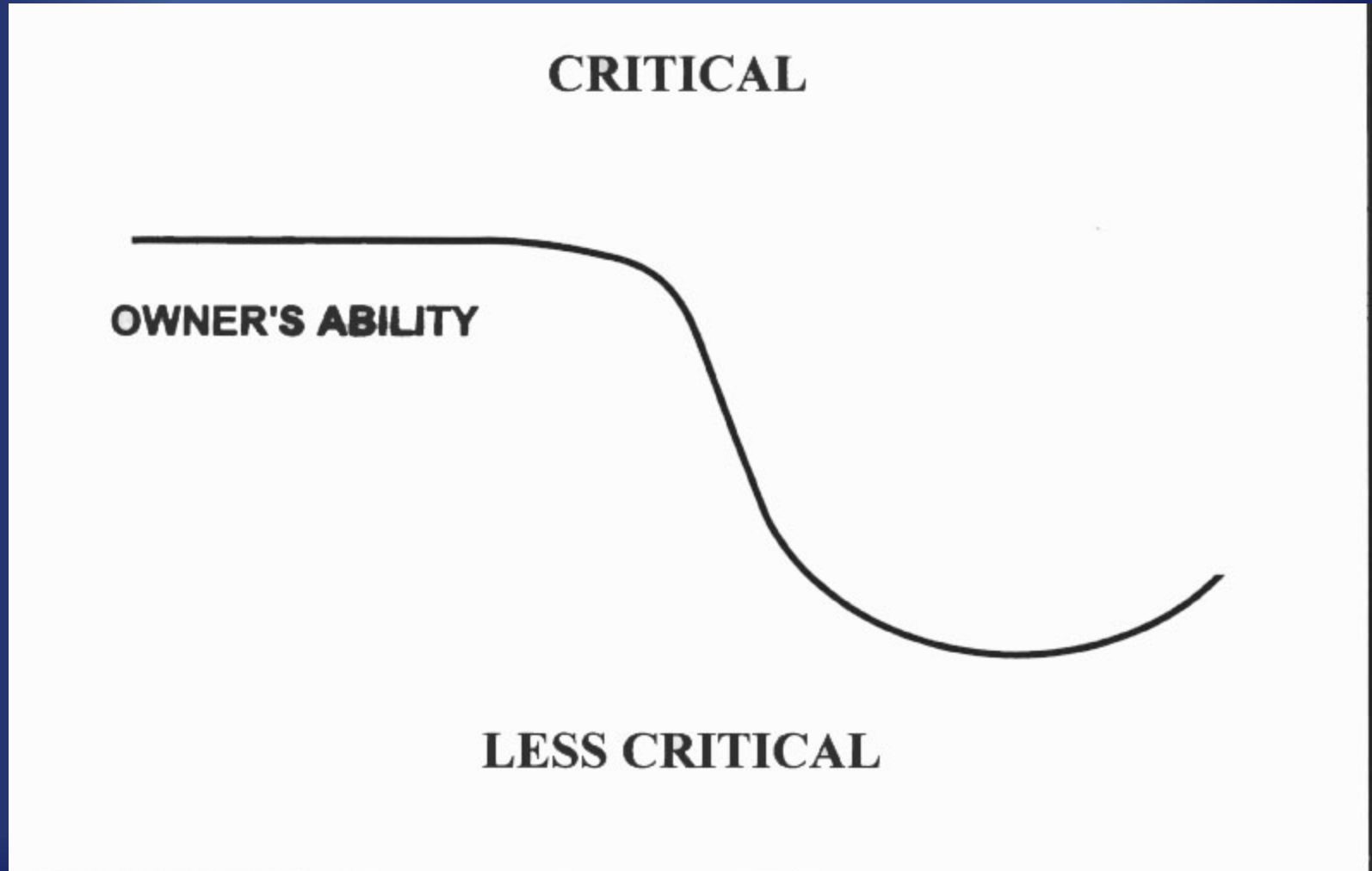
CRITICAL

LESS CRITICAL

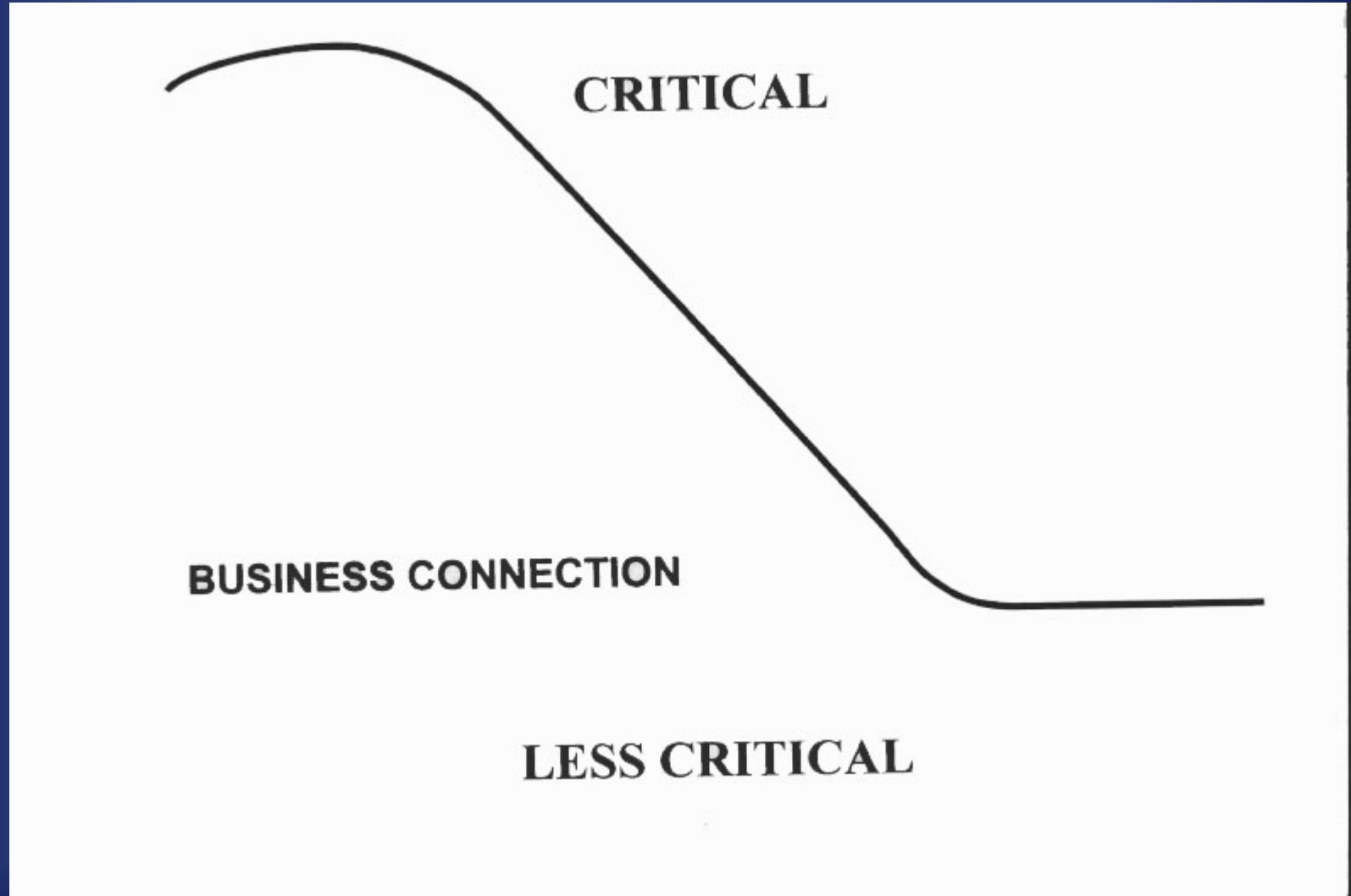
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STARTUP SURVIVAL SUCCESS GROWTH MATURITY

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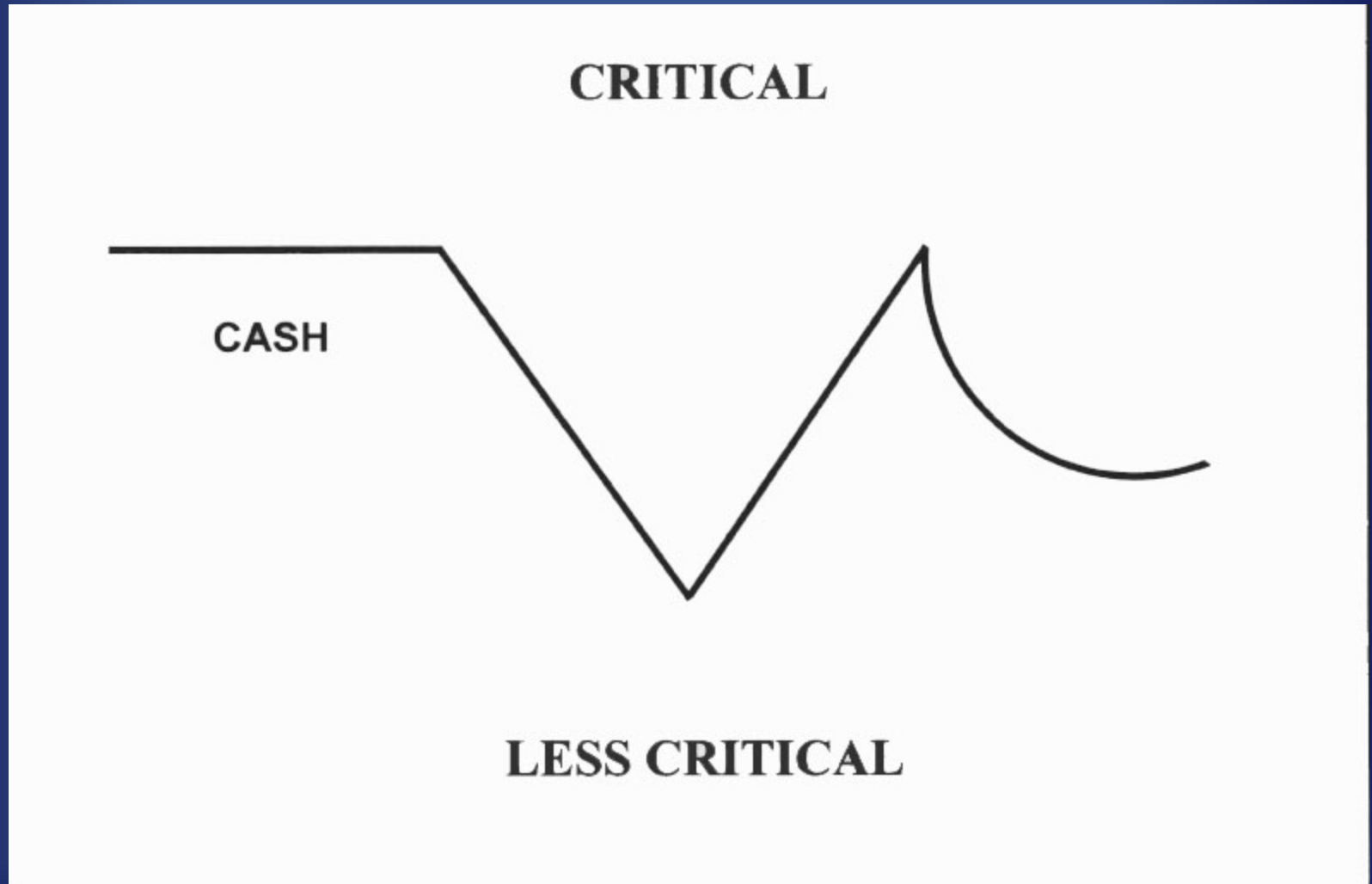
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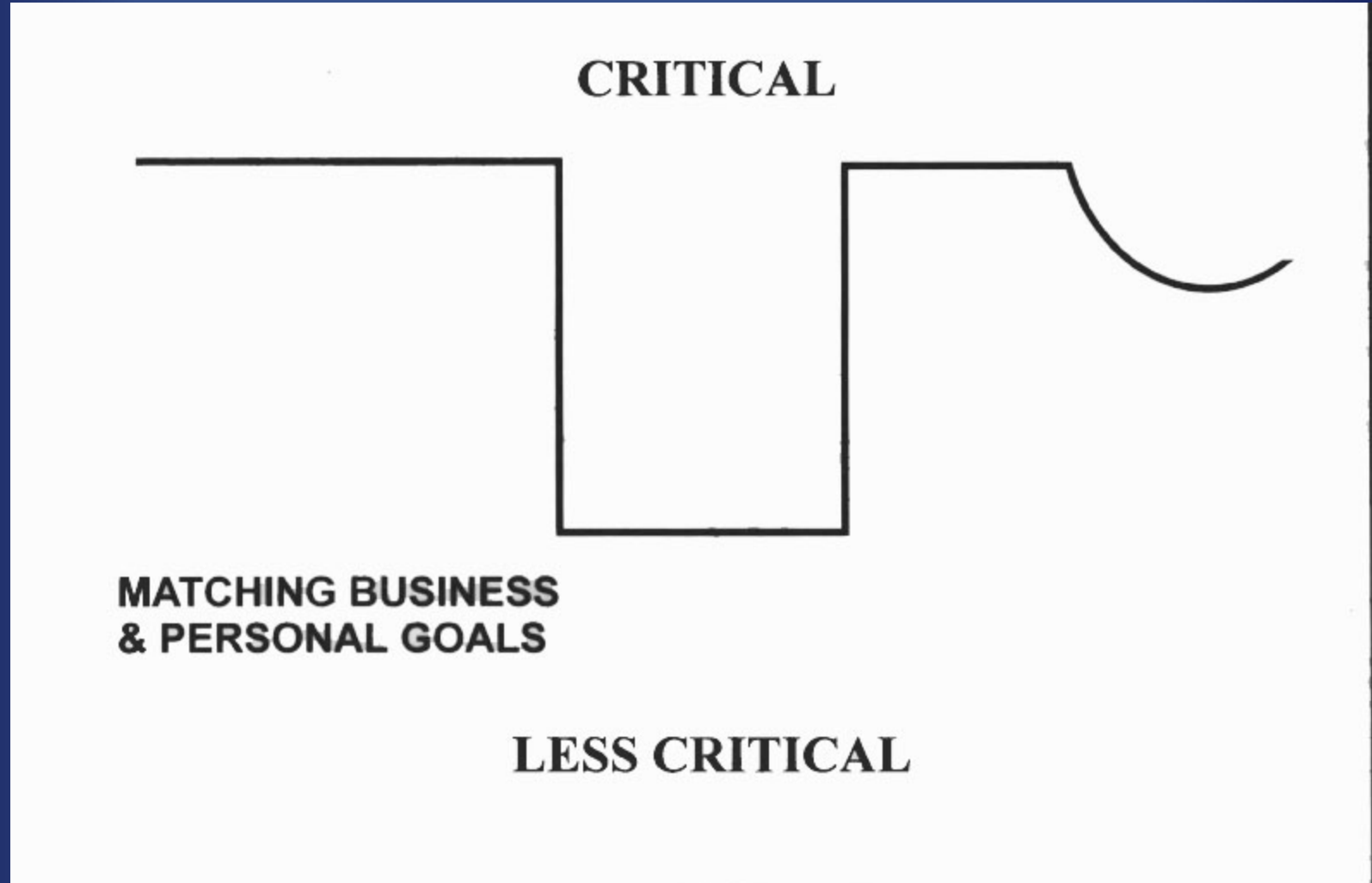
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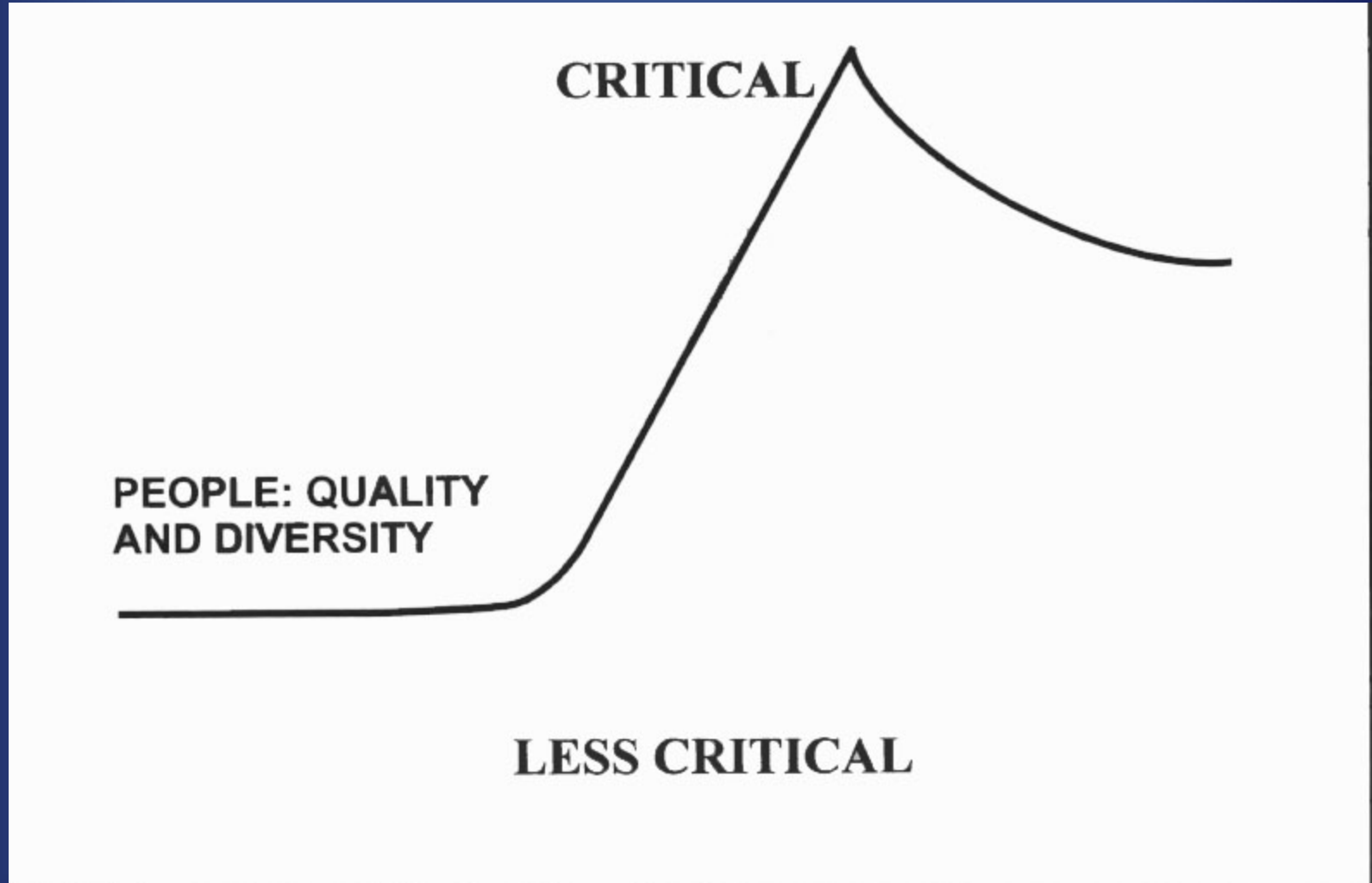
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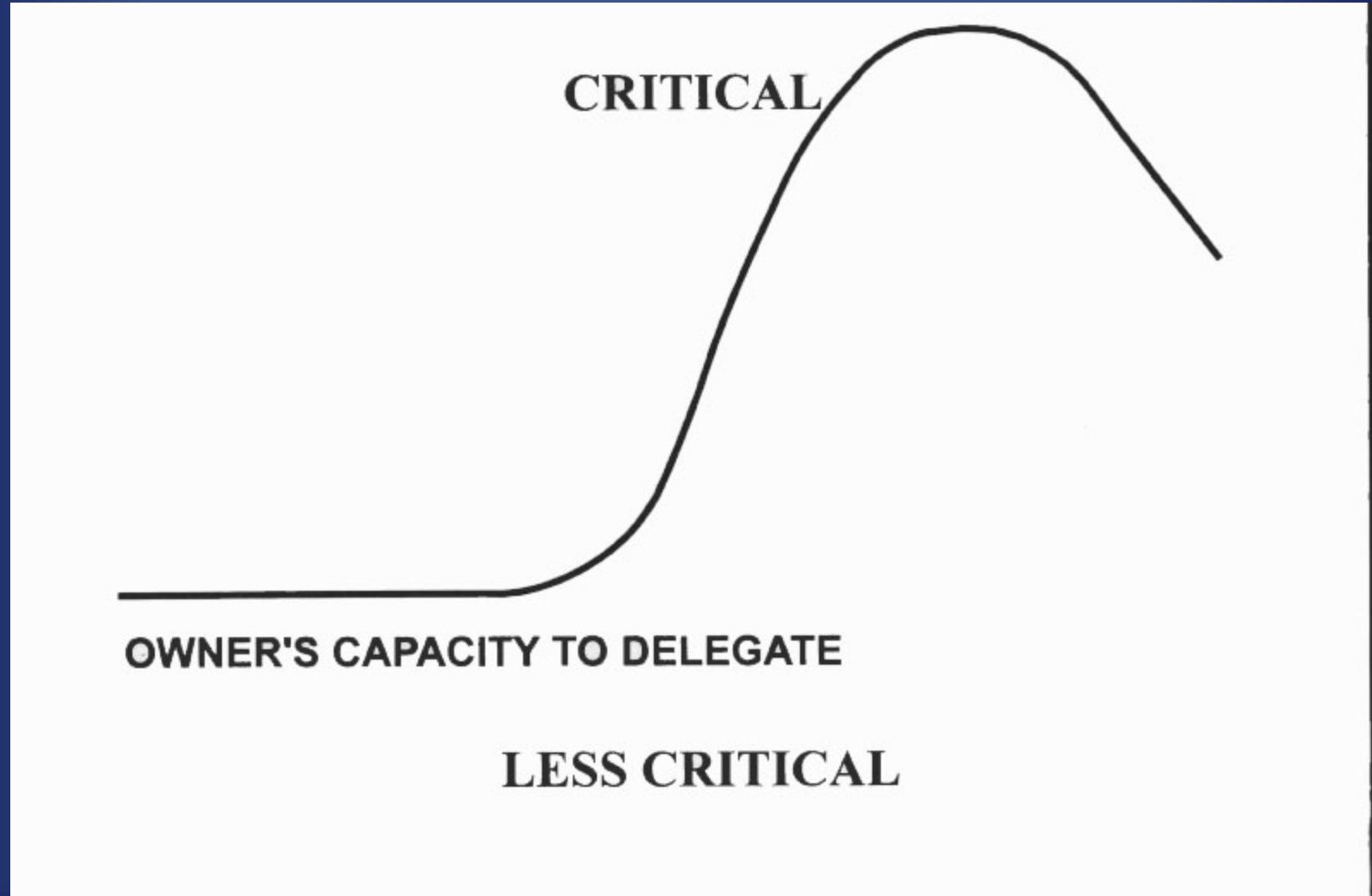
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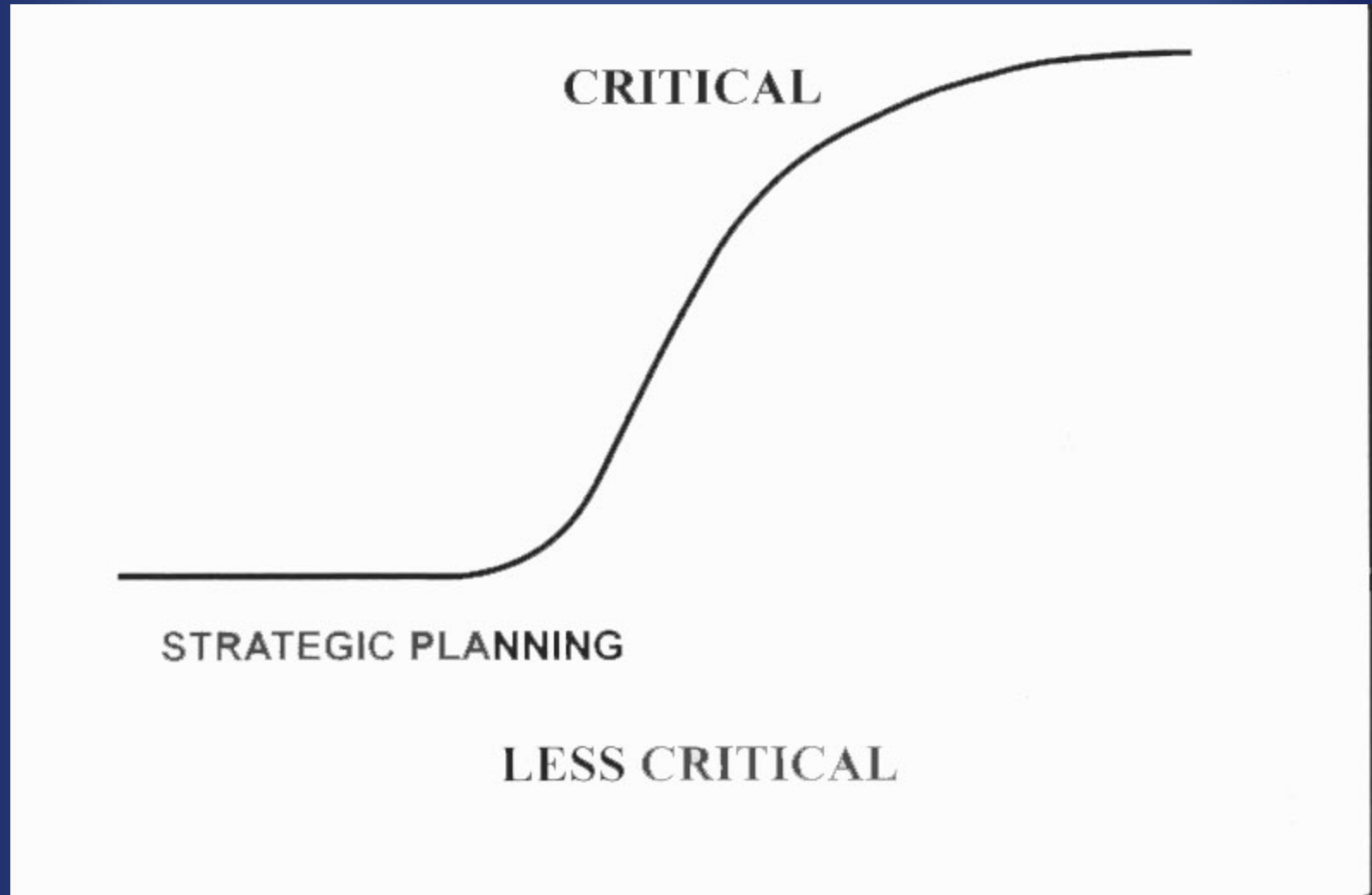


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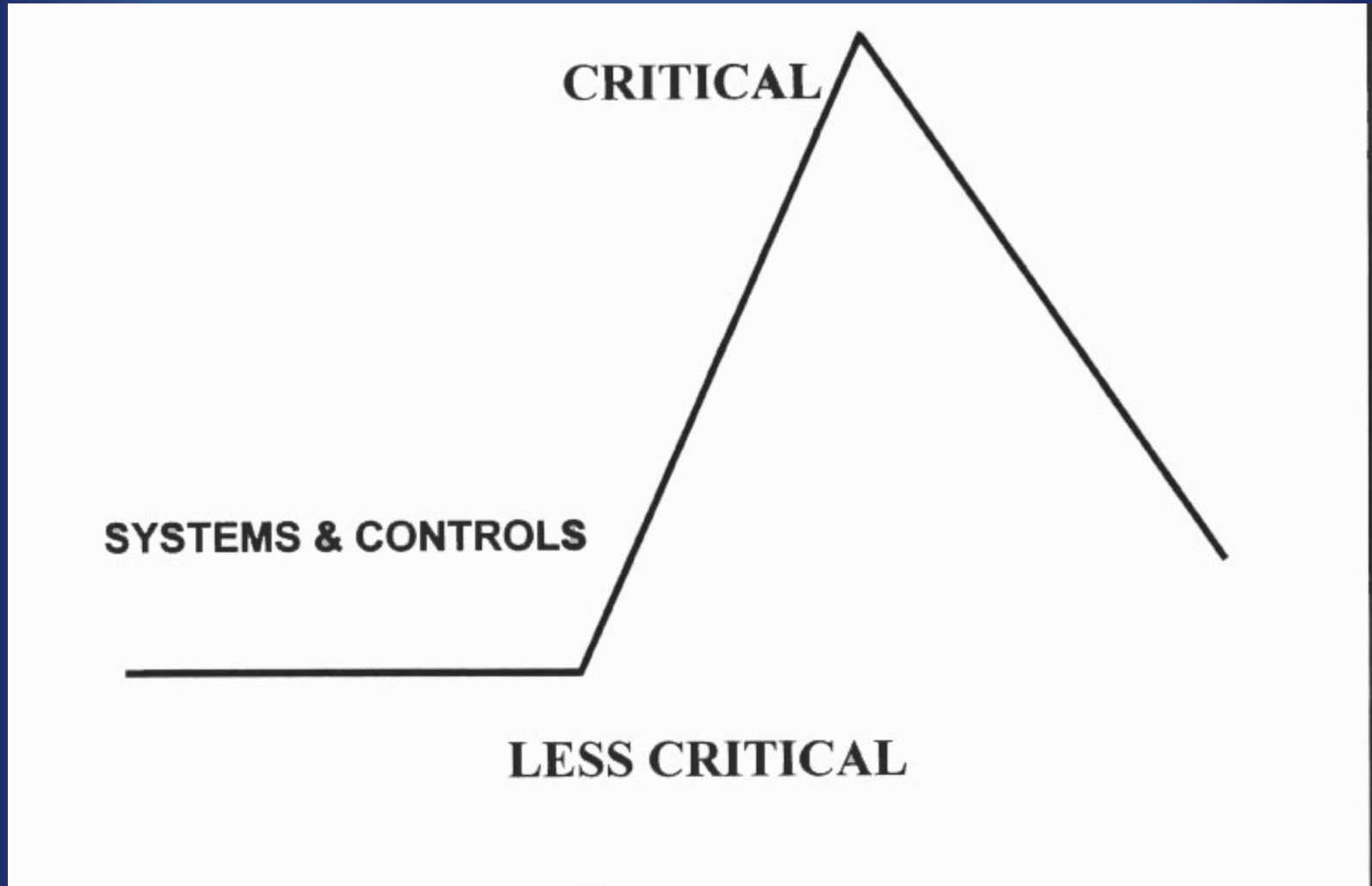
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GROWTH

- **More Work versus More Profit**
- **Fundamental Rule of Profit versus Value**
- **Healthy Growth Centers around Capital Accumulation**
- **The Link between Capital, Technology and Growth**
- **Risk of Growth Outstripping Capital Replenishment**

John Murdough on Growth Cycles

- Bad jobs, customer problems, fading margins
- Problems: cash flow, underbillings, A/R, debt
- Slow and poor information; delayed billings
- Increased capital expenditures
- Over comp, turnover, stress, lack of training
- Early: profit up, OH down, ratio stress
- Later: profit fades, ratios extreme stress

Indicators of Market Slipping

- Imbalance of large and small projects
- Margins slipping
- Increase in number of bidders/competitors
- Unusual competitors not seen before
- Increase in extremely low bids
- Credit tightening

Prevention Strategies

Profit not Volume: Downsize-Timing
(Not Dismantling)

Flexible Overhead (stair step)

Accountability

Board of Directors/Advisors

Prevention Strategies

- Advantages of Training and Education
- Embracing New Technologies
- Planning—Flexible OH

Be Proactive

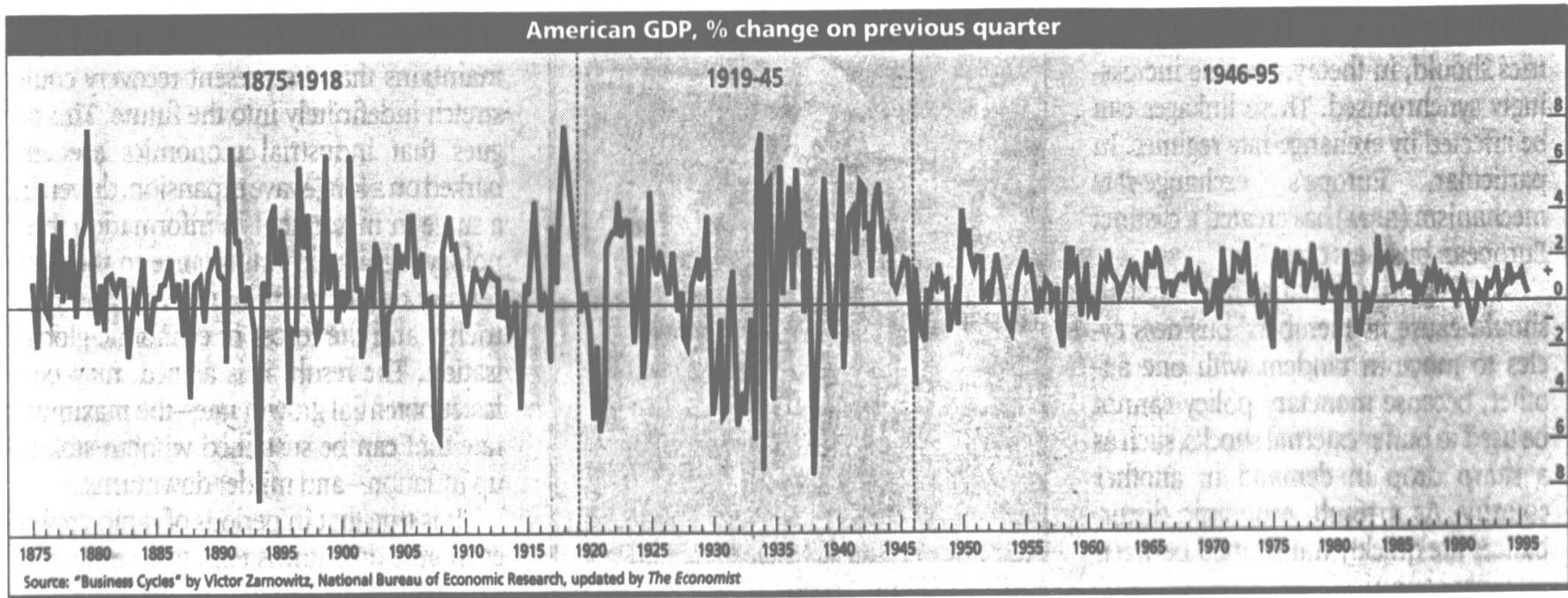
- Focus on good clients--weed out
- Best type of work—best people
- Improve technology and systems
- Repair and plan replace equipment
- Train, Train, Train

Measure Results

- Operational vs. Financial Performance
- Return on Investment
- RScore

Historic Perspective

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Our Economic Future

- 4.5% world population—80% Nobel Prizes
- Responsible for 90% most important inventions in last 100 years
- Creates 1/3 of the Gross World Product
 - US GDP \$12 trillion—GWP \$37 trillion (est.)
- Consumer net worth, \$50 trill
 - Room for growth—half people in world make less \$2/day
 - 3 billion people have never used a telephone

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QUESTIONS/COMMENTS