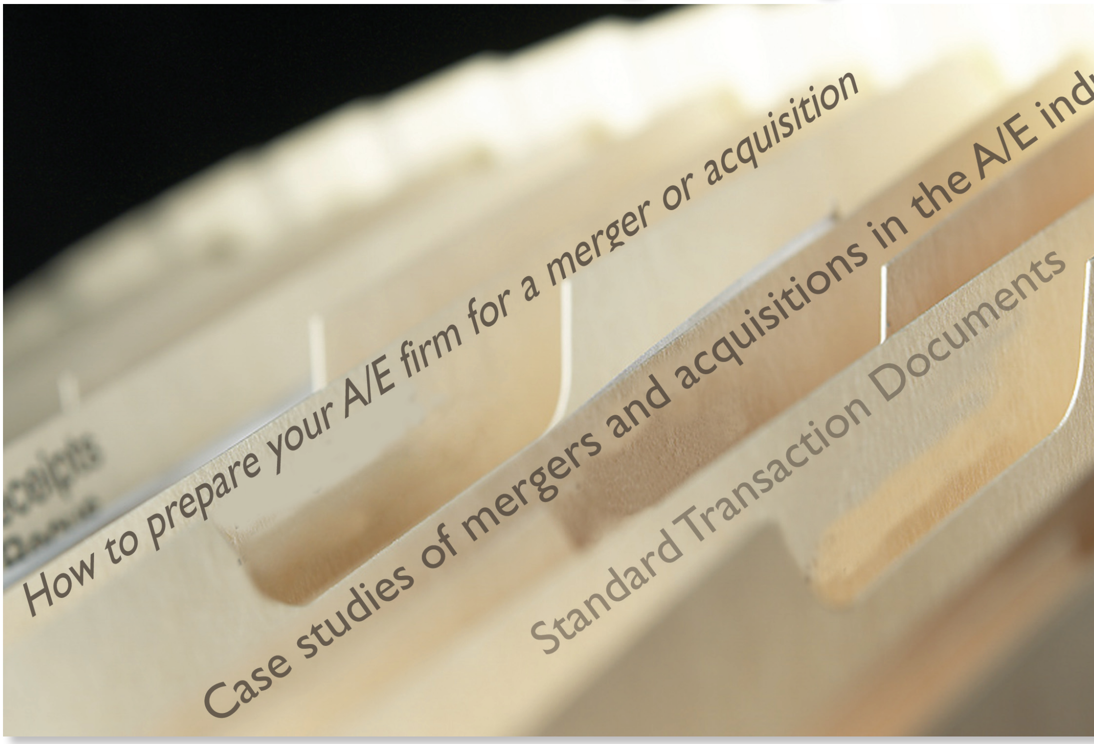
# Consolidation of Engineering Firms




By Thornton J. Williams, Williams McMillian P.A.

Consolidation has been a dominant theme in the engineering sector for the past several years. In a 2006 article, entitled, "Consolidation in the Engineering Industry," it was reported that engineering industry's revenues had reached record heights and the industry had become very fragmented and was now consolidating. Based on those factors, it was the optimal time for engineering firms to sell and align with larger entities.

Larger firms were leveraging their significant cash positions to acquire smaller firms for increased market share, new customers, additional engineers, new geographic territories, economies of scale, and growth.

But what does the engineering industry forefront look like today after the recession of 2008 which began a major worldwide economic downturn that continued into 2010?

Although the U.S. economy has stabilized it has not shown signs of significant recovery yet, with serious weaknesses continuing in housing, employment, commercial real estate, banking, automobiles, and retail trade. Engineering firms have had to endure the downturn as much as any industrial segment and in some instances have had to consolidate for survival.

The number one limitation of growth for engineering firms is a shortage of qualified engineers. Add to that equation the fact that engineering firms today face increasing pressure to accelerate product time-to-market, deliver more high-quality products to customers and reduce overall costs. With the increased marketing costs required to win projects and increased recruiting costs to hire new engineering talent, achieving these goals is prompting increased evaluation by engineering firms of the benefits of consolidation and in turn, we are seeing smaller engineering firms merging their business with larger entities which have more substantial systems and resources in place.

According to a CEO survey published in 2010 by Farkas Berkowitz & Company, "71 percent of engineering firm CEOs think the pace of consolidation in the engineering industry will increase over the next decade, and 59 percent expect it to increase in the construction industry. In addition, over half of the survey participants see consolidation as the most significant force affecting the engineering and construction industry over the next 10 years."

Consolidation holds many potential benefits for companies that can achieve it. However, in today's economic climate, is bigger really better?

Strategically, consolidation allows companies to shift engineering capacity more readily to meet the engineering resources requirements across their business. However, according to the *Engineering News Record* (*ENR*) Top 500 Design Firm Survey of 1999, for most markets, the largest firms saw revenues decline more sharply than their smaller competitors.

Moreover, while analysis of the *ENR* survey data showed the top five firms in the transportation, water-wastewater, and hazardous waste (remediation) markets saw their market shares increase significantly relative to their smaller competitors, among environmental and infrastructure engineering markets, power engineering went in the opposite direction.

PricewaterhouseCoopers offers helpful questions for consideration by engineering firms contemplating consolidation (mergers and acquisitions). Some of the essential questions include:

- How well does the target company support the company's corporate strategy?
- What cultural clashes might arise as the two companies come together?
- How competent is the target company's management? How easy will it be to work with?
- How skilled are the workers?
- Was revenue restated, and if so, why?
- Is the company involved in litigation?
- Are there any warranties—written statements from the seller that confirms a key fact about the target's business?
- Are there any indemnities—commitments from the target company to reimburse the buyer in full in certain situations?
- Can the company mitigate its risk through deal structuring and/or contractual protection?
- Does one of the merged companies have products with a quality or reputation that can harm the reputation or perceived value of products offered by the other merged company?

It is obvious that the decision to merge is a significant one that requires a lot of due diligence by engineering firms seeking to increase their costs benefits, avert failure and grow their business.

Undoubtedly, consolidation has been a major force for some time and will continue to be one in the future. ■

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