Session 1: An Overview of the Dynamics Driving The New Landscape

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PROGRAM CO-CHAIR
New Dynamics Impacting the EPC Landscape?

The Past 6 Years Were Drastically Different From The Prior 25
What Does The Future Hold?
General Session

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Session 1: An Overview of the Dynamics Driving The New Landscape
Gaining Advantage In A Dynamic Project Environment

PAUL BARSHOP
Chief Operating Officer
Independent Project Analysis
The excessive asset, commodity and economic volatility witnessed during 2007-2010 have professional investors rethinking past strategies, challenging beliefs, and focusing more on what can go wrong, rather than the possibilities of what can go right.

Will an investment in an engineering contractor provide a rate of return greater than alternative opportunities? How will this impact this industry on a global basis?

- Prove its Ability to Manage the Downturn/Pause
- Stressing Risk Mitigation in Face of Severe Competition
- Allocate Resources to Businesses That Can Generate Returns
During the past six years, which industry sector share prices have been the best performing?

1. Chemical 8%
2. E&C 8%
3. Mining 23%
4. Oil 33%
5. Oil Service 15%
6. S&P 500 13%
All About The Share Price
All About The Share Price

- Clients and Vendors Outperformed the Market
- Mining Better than Big Oil/Chemical
- E&C Equities Rode the Wave
Prove Ability to Manage Downturn

- Margin Improvement Early – Cyclically Pressured
- Profit Productivity a Key
- Late Cycle Fears Prevalent
Risk Mitigation

- LSTK – Market Driven, but Can E&C Firms Manage?
- Forgo Backlog Growth for Profit Growth? Can it be Done?
- Focus on Mix, High Value Content, Free-Agents, Technology

Backlog Mix - LSTK vs. Cost Plus

- LSTK
- Cost Plus

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<th>Cost Plus</th>
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Allocation of Resources

- Metals & Mining - The Next Long Up-Cycle
- Government - Still Need to Defend and Regulate
- Infrastructure – Can Public-Private Partnership Model Gain Traction in the US?
The Market Wants Companies To...

- Eliminate “Above the Fold” Negative Events
- Efficiently Manage Professionals to Catch the Next Cyclical Wave
- Extract “At-Least” Fair Value from Clients
- Evaluate Excess Capital and Allocate Wisely
- Exceed Profit and Return Levels Achieved During 2007-08
BUSINESS AS UNUSUAL

Gaining Advantage in a Dynamic Project Landscape

SEPT. 1ST–4TH 2010

RITZ CARLTON GRANDE LAKES

ORLANDO, FLORIDA

42ND ANNUAL ECC CONFERENCE
Another Hot Market On The Horizon?

Level of megaproject activity 2000 - 2015

Rate of projected growth is faster than 2004 to 2007 period

Limited View of Projects Entering FEL 2 in 2010-12

Forecast for megaproject spending

Source - IPA EPC Market Forecast Newsletter

Global onshore capital projects greater than $1 Billion

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Composition of Megaproject Spending Forecast

**NUMBER OF PROJECTS**

- PetroChem: 28%
- Refining: 29%
- Gas: 18%
- LNG: 17%
- Other: 8%

**CAPITAL SPEND BY SECTOR**

- PetroChem: 22%
- Refining: 27%
- Gas: 15%
- LNG: 28%
- Other: 8%
ARS Question

What is your view on megaproject spending during the next several years relative to my forecast?

1. More than the forecast
   - 9%

2. About equal to the forecast
   - 26%

3. Somewhat less than the forecast
   - 65%
ARS Question

Over the next 5 years how do you expect prices for capital projects to react compared to the last hot market:

1. Escalate as fast or faster 10%
2. Escalate, but not as great a rate (more historical rates) 49%
3. Stay relatively flat 33%
4. Decline 8%
Neither Beginning Nor End Of Recent Hot Project Market Was Anticipated

Projects authorized from 2004 to 2006 overran

Long period of price stability

Projects authorized after mid-year 2006 are underrunning

Source – IPA’s Process Plants Database

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Coping In A Dynamic Project Environment

- There is a desire for engineering organizations to function effectively in a dynamic project environment.

- Being able to cope in a dynamic environment means the owner engineering organization can better support the businesses they serve.

- Unfortunately, the owner’s success rate in a dynamic project environment isn’t very good.
Examples Of Difficulty
In a Dynamic Project Environment

- Cost overruns in the hot market
- Expensive first-to-region projects
- Finishing alternative selection on time
First-to-Region Projects Tend To Be More Expensive

A company first to region project is typically 6 percent more expensive than projects done in the same location by companies with experience in the region.

Source – IPA’s Process Plants Database
Project Teams Have Difficulty Finishing FEL 2 When Alternatives Are Evaluated

Alternative selection is the formal comparison of different options for maximizing an investment’s business results.

Data from IPA Process Plants Database

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Gaining Advantage In A Dynamic Project Environment Requires Investment

- Owner companies with the capability to develop cost estimates in-house had 5 percent less average cost growth each year from 2003 to 2007.

- First to region projects that completed extensive location studies during project development achieved competitive cost results.

- Availability of owner engineering resources to frame alternatives and lead the evaluation of alternatives lowers the frequency of incomplete FEL 2.
Other Important Capabilities for Dynamic Times

- Flexibility to select and execute multiple contracting strategies
- Gather independent market intelligence on contractor and vendor capability, prices, and quality
- Capability to provide comparative estimates to quickly screen options
- Ongoing studies of developments in processing / manufacturing technology
Contractors Are Doing It – Are Owners?

- Mike Dudas reports that the market expects engineering and construction contractors to invest cash wisely and be ready to catch the next wave of investment.
- Are owners sufficiently investing in people and tools to be ready to operate in dynamic project environment?
- Do owners have enough resources for the following?:
  - Continuously survey the project environment to identify changes with enough lead time to react.
  - Support the decision-making process that shapes business opportunities and determines the optimal project scope.
  - Manage projects to achieve business objectives at the lowest possible capital cost.
Are owner organizations investing in their internal project delivery capability sufficiently to excel in a dynamic project environment?

1. Yes, in most areas
   - 9%

2. Mixed, some investment areas
   - 39%

3. No, some investment, but it is not enough
   - 52%
ARS Question

Pick The Three Dynamics That Will Have The Greatest Impact On The E&C Industry Over The Next Five Years

1. Greenhouse Gas Issues 16%
2. Global Economic Recovery 33%
3. Labor Availability 17%
4. Material Availability 6%
5. Price Of Oil 23%
6. Other 5%
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