

# BUSINESS AS UNUSUAL

Gaining Advantage in a Dynamic Project Landscape



PROGRAM CO-CHAIR

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

**MIKE LOWDER**

Eastman Chemical Company

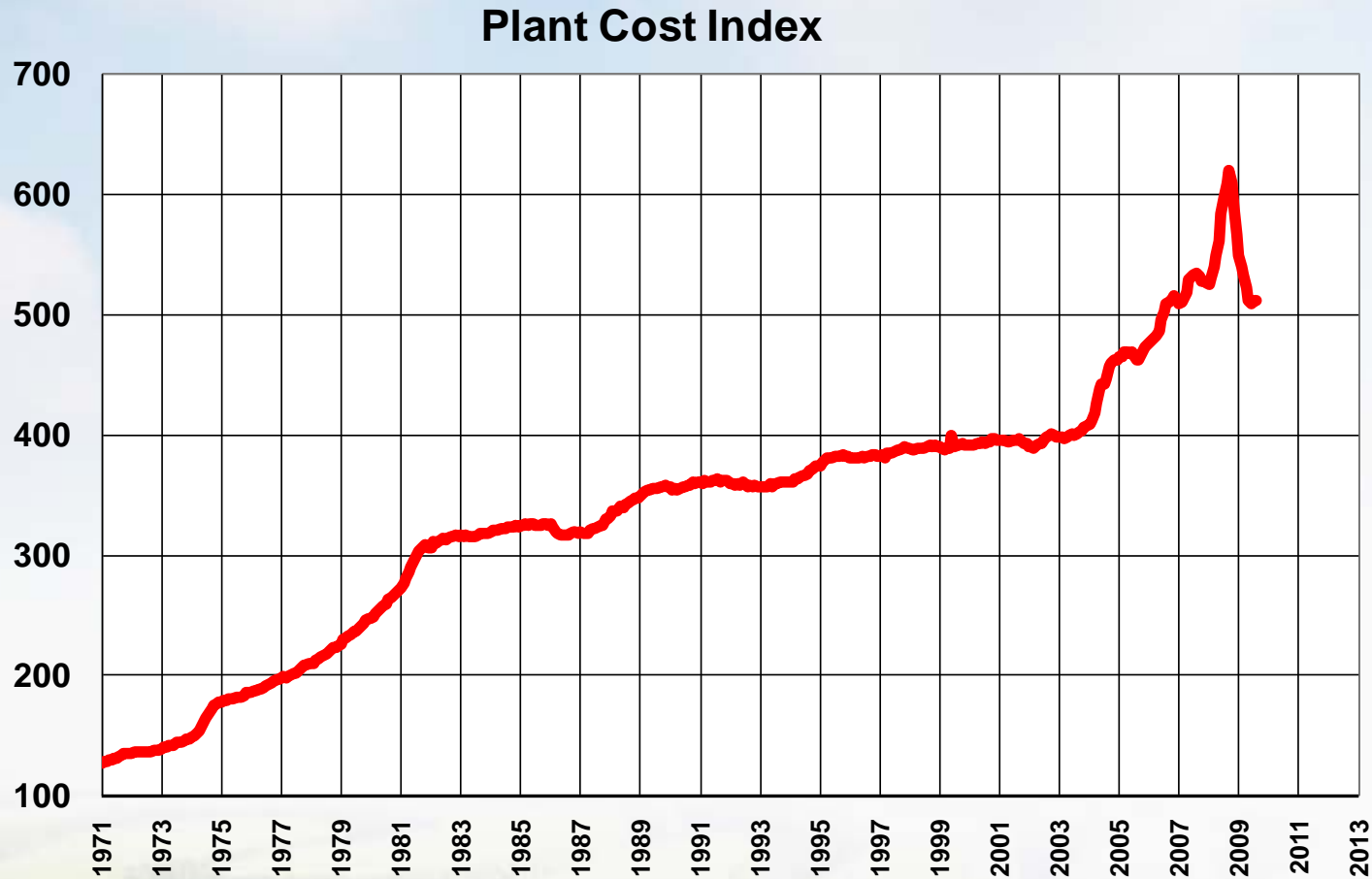


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# New Dynamics Impacting the EPC Landscape?



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

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

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## Gaining Advantage In A Dynamic Project Environment

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# What Do E&C Shareholders Expect From Management?

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**

# ARS Question

During the past six years, which industry sector share prices have been the best performing?

1. Chemical



2. E&C



3. Mining



4. Oil



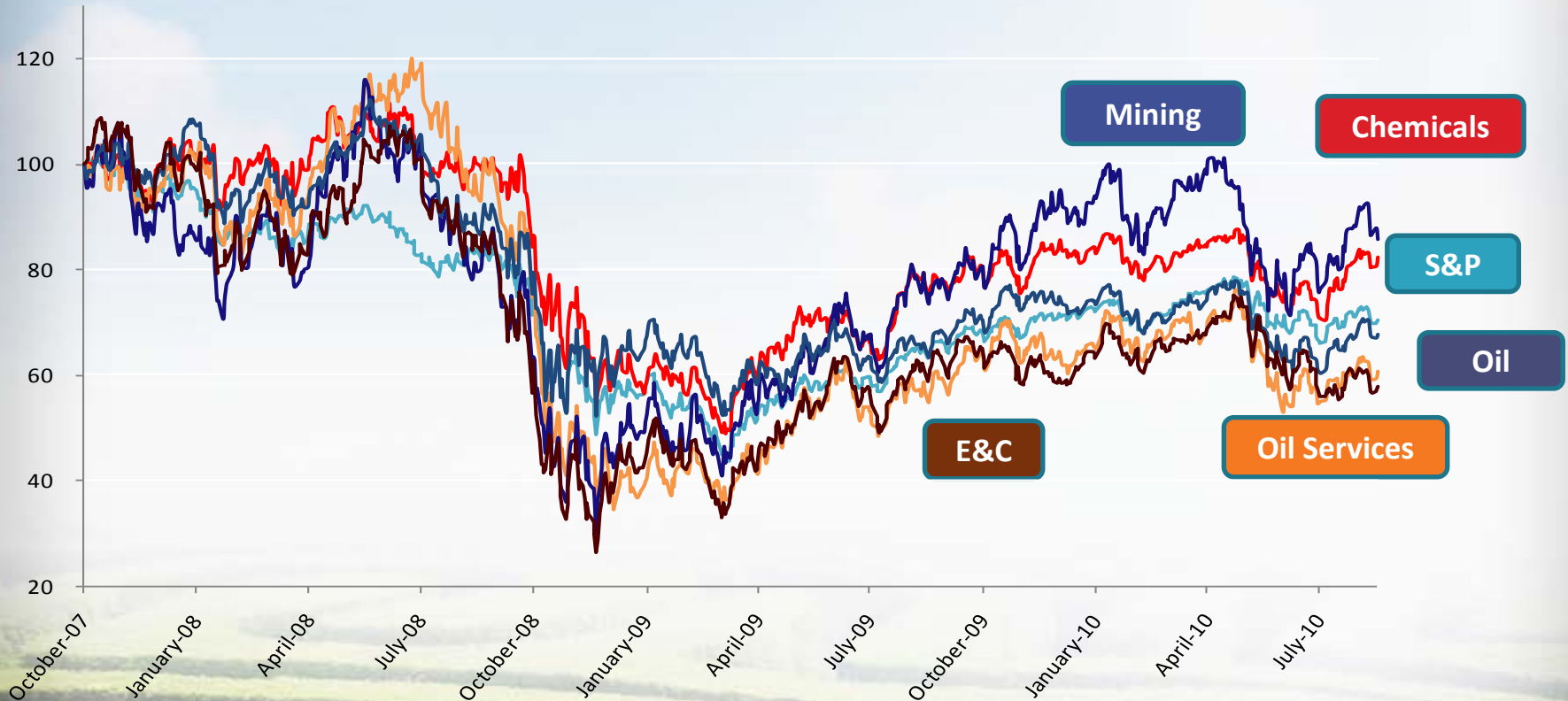
5. Oil Service



6. S&P 500



# All About The Share Price





# All About The Share Price

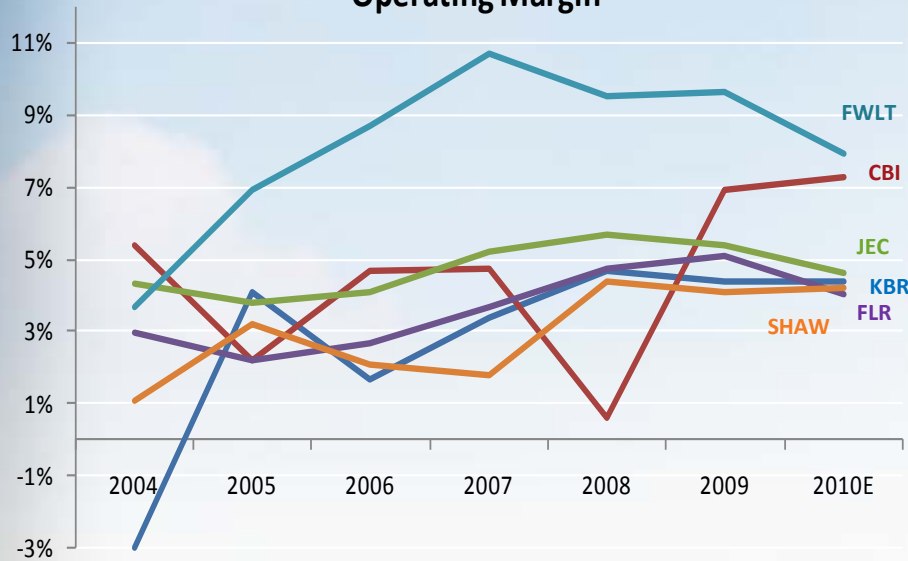


- Clients and Vendors Outperformed the Market
- Mining Better than Big Oil/Chemical
- E&C Equities Rode the Wave

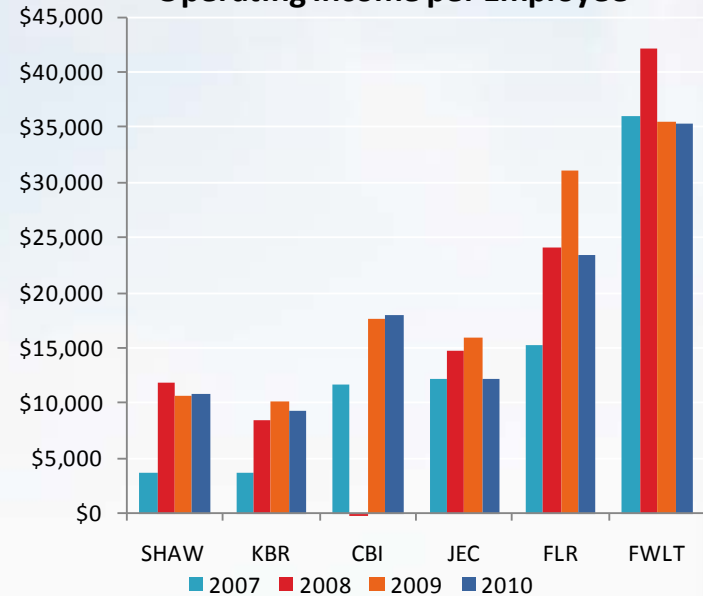


# Prove Ability to Manage Downturn

Operating Margin

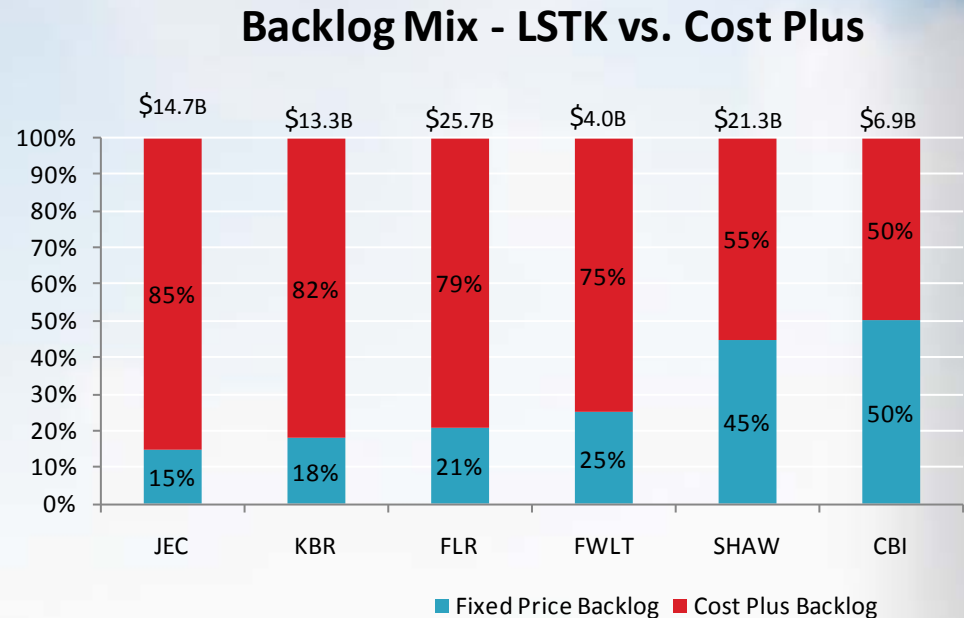
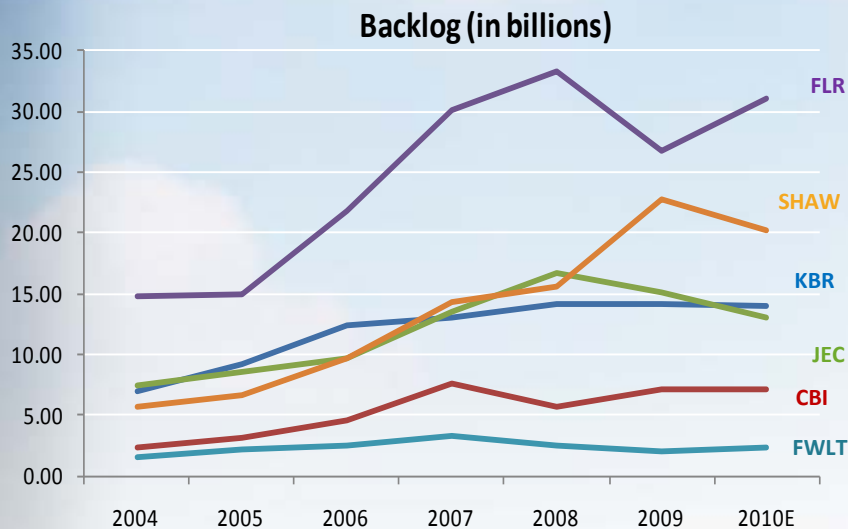


Operating Income per Employee



- 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

# Allocation of Resources

Commodity Prices 2004-2010



- 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



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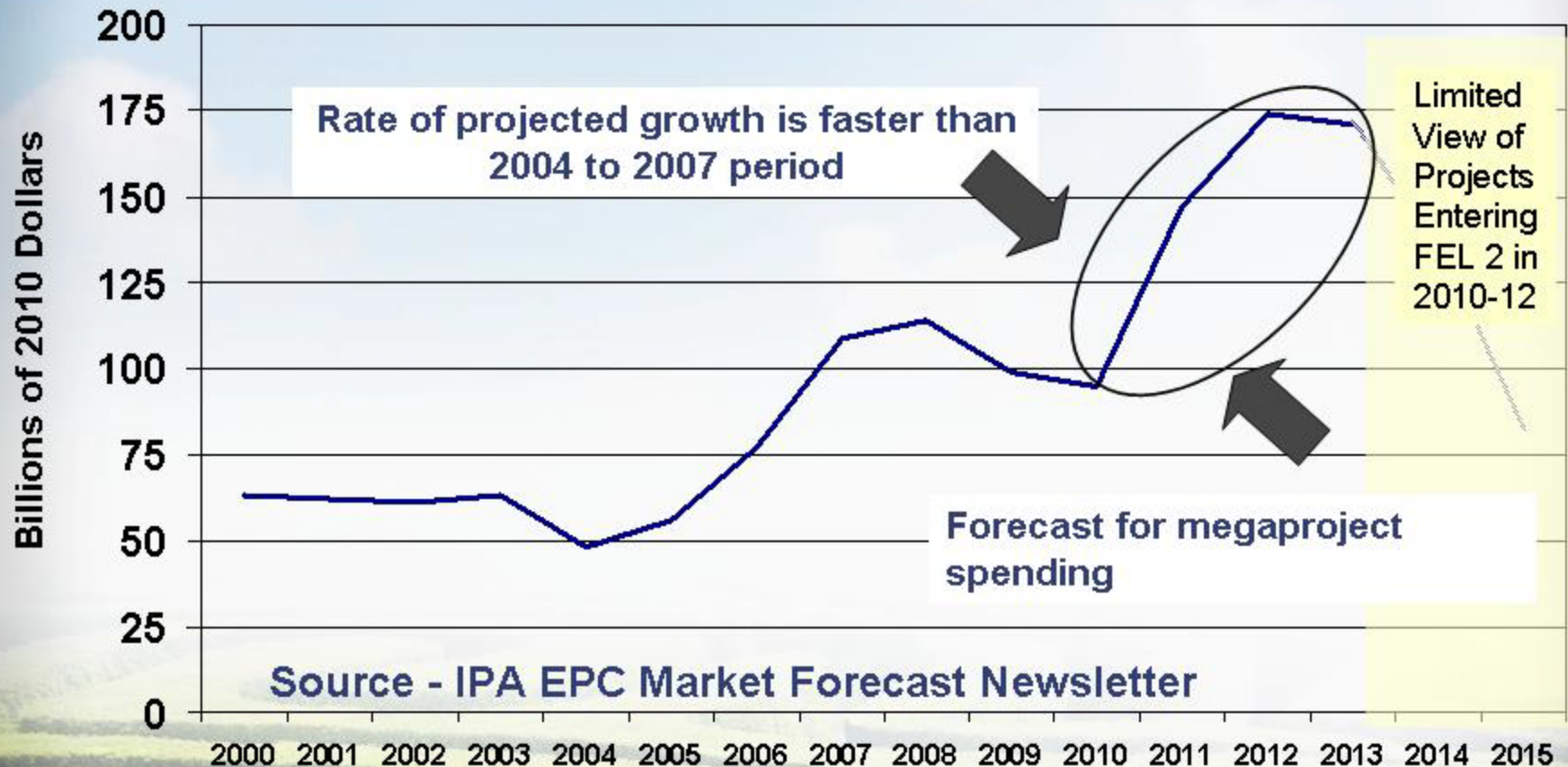
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# Another Hot Market On The Horizon?

Level of megaproject activity 2000 - 2015

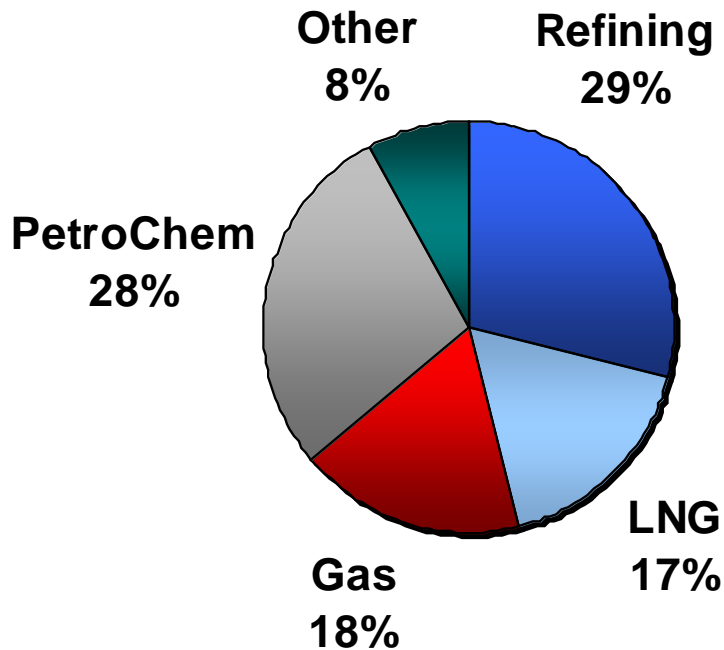


Global onshore capital projects greater than \$1 Billion

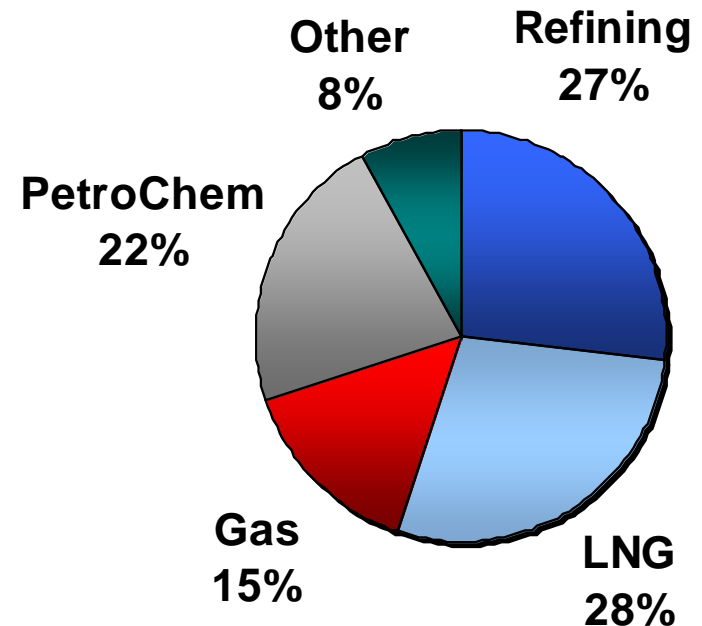


# Composition of Megaproject Spending Forecast

NUMBER OF PROJECTS



CAPITAL SPEND BY SECTOR



# ARS Question

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

1. More than the forecast



2. About equal to the forecast



3. Somewhat less than the forecast





# 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%

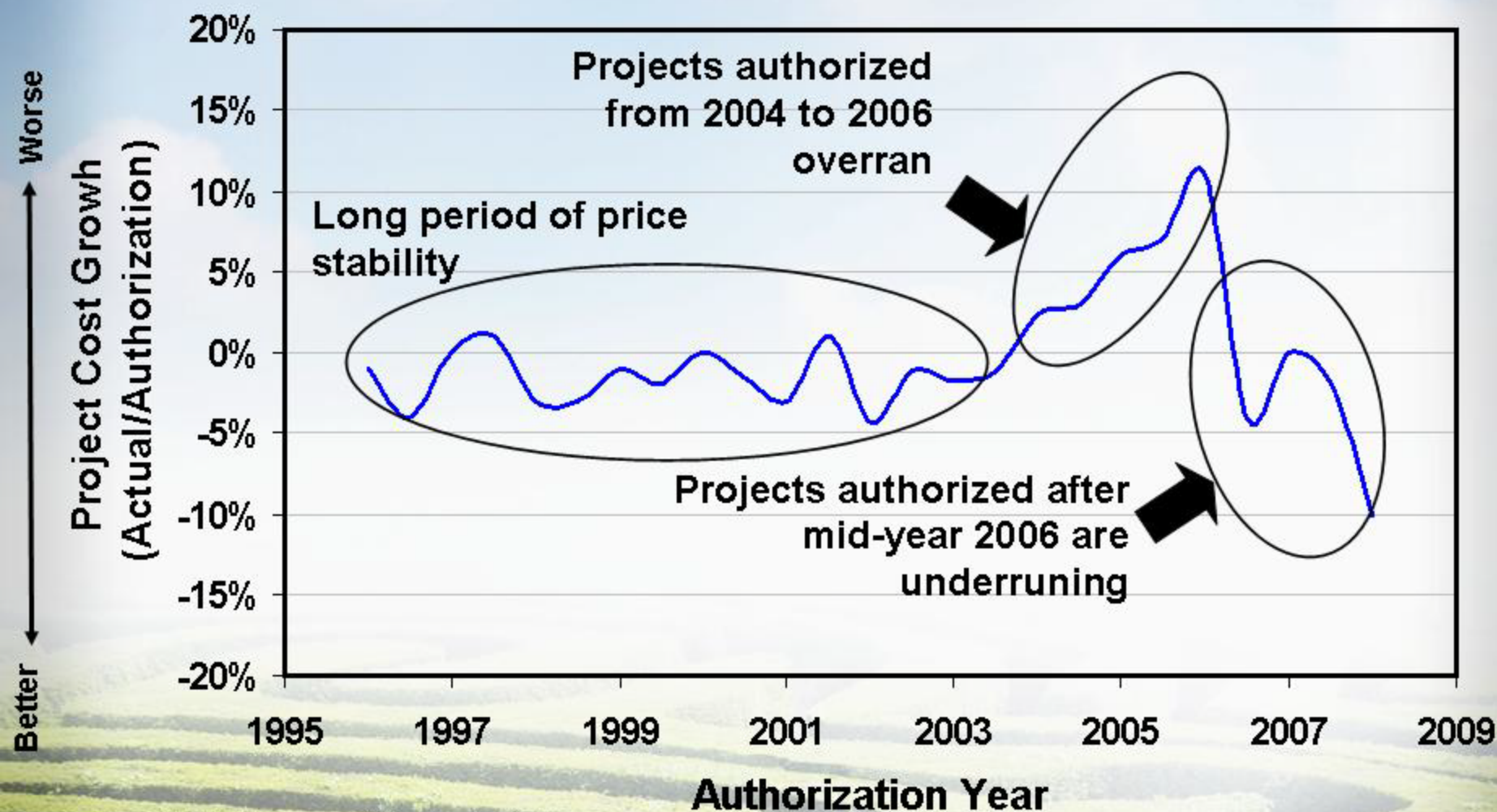
3. Stay relatively flat

 33%

4. Decline

 8%

# Neither Beginning Nor End Of Recent Hot Project Market Was Anticipated



Source – IPA's Process Plants Database

# 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

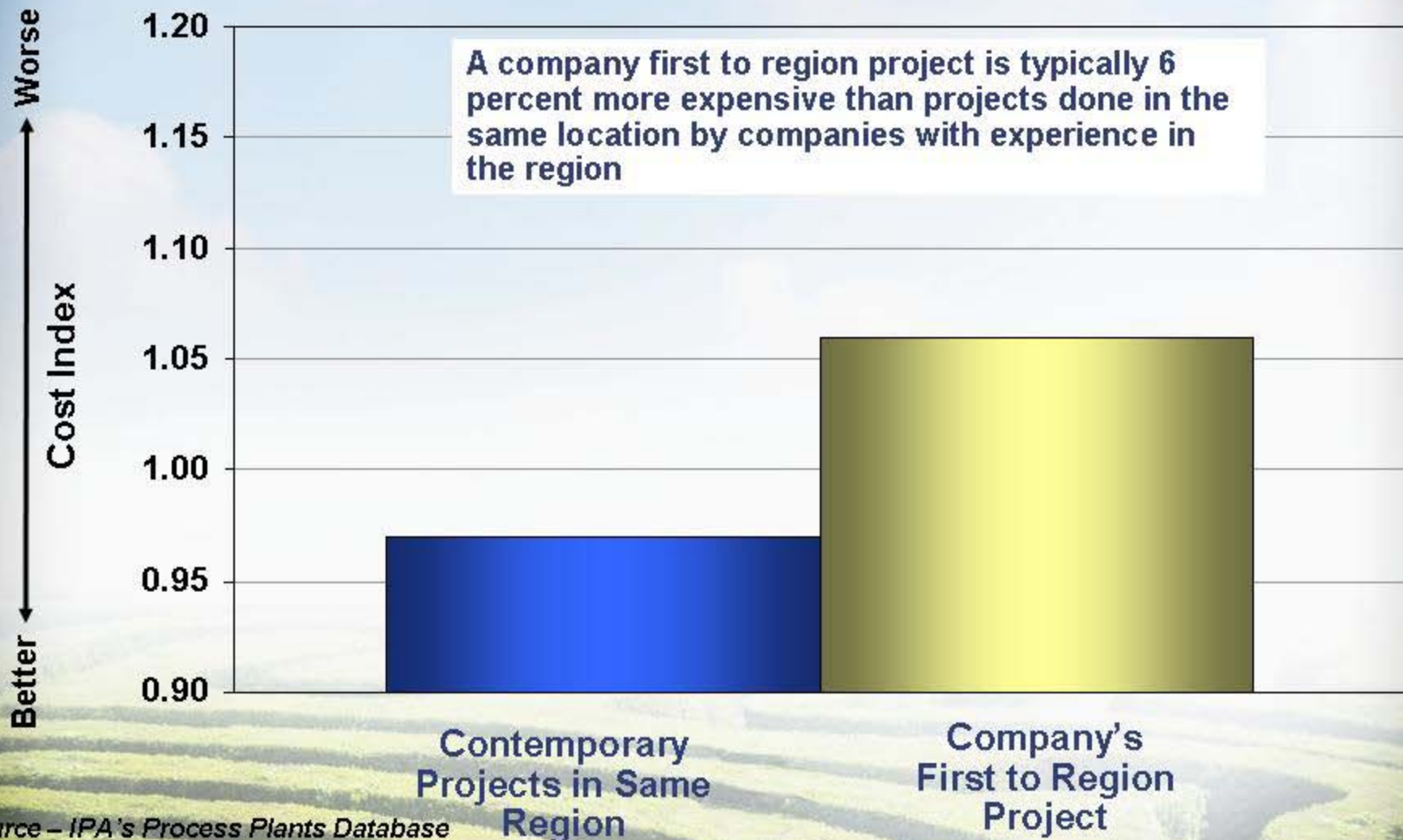


# Examples Of Difficulty In a Dynamic Project Environment

- Cost overruns in the hot market
- Expensive first-to-region projects
- Finishing alternative selection on time

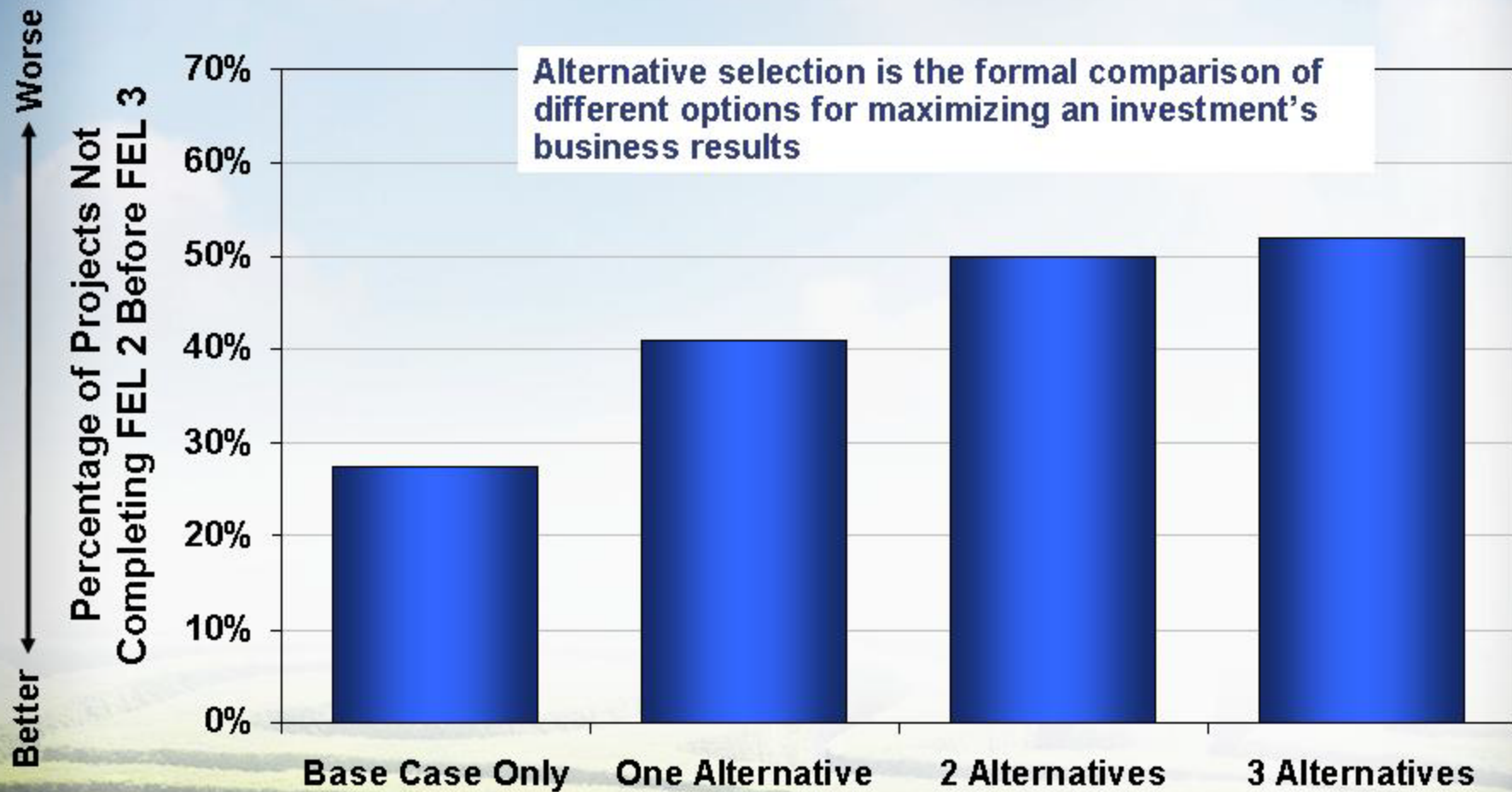


# First-to-Region Projects Tend To Be More Expensive



Source – IPA's Process Plants Database

# Project Teams Have Difficulty Finishing FEL 2 When Alternatives Are Evaluated



Number of Alternatives Evaluated in FEL 2

Data from IPA Process Plants Database

# 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

# ARS Question

Are owner organizations investing in their internal project delivery capability sufficiently to excel in a dynamic project environment?

1. Yes, in most areas



2. Mixed, some investment areas



3. No, some investment, but it is not enough



# 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



2. Global Economic Recovery



3. Labor Availability



4. Material Availability



5. Price Of Oil



6. Other





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