

How to Prepare for a Changing Infrastructure Market

By **Brian Moore**

With 2021 infrastructure investment likely to remain the same as 2020, companies need to prepare for fewer opportunities for growth and increased competition. Here are six steps all heavy civil contractors should be taking now to prepare themselves for the challenges ahead.

According to our most recent peer group benchmarking, most heavy civil and highway contractors saw positive performance in 2020 despite negative factors like the global pandemic and a national recession. Similar to consumer packaged goods (CPG) companies, e-commerce and other sectors, heavy civil firms entered 2020 with strong project backlogs and bright prospects for the year.

While some experienced temporary pauses in early 2020 due to work shutdowns, most civil construction work was quickly deemed essential. Many companies were able to complete work faster because of reduced traffic, which meant they burned backlogs quicker than expected. The net result, for many, was a good year, despite the challenges, with strong backlogs heading into the beginning of 2021.

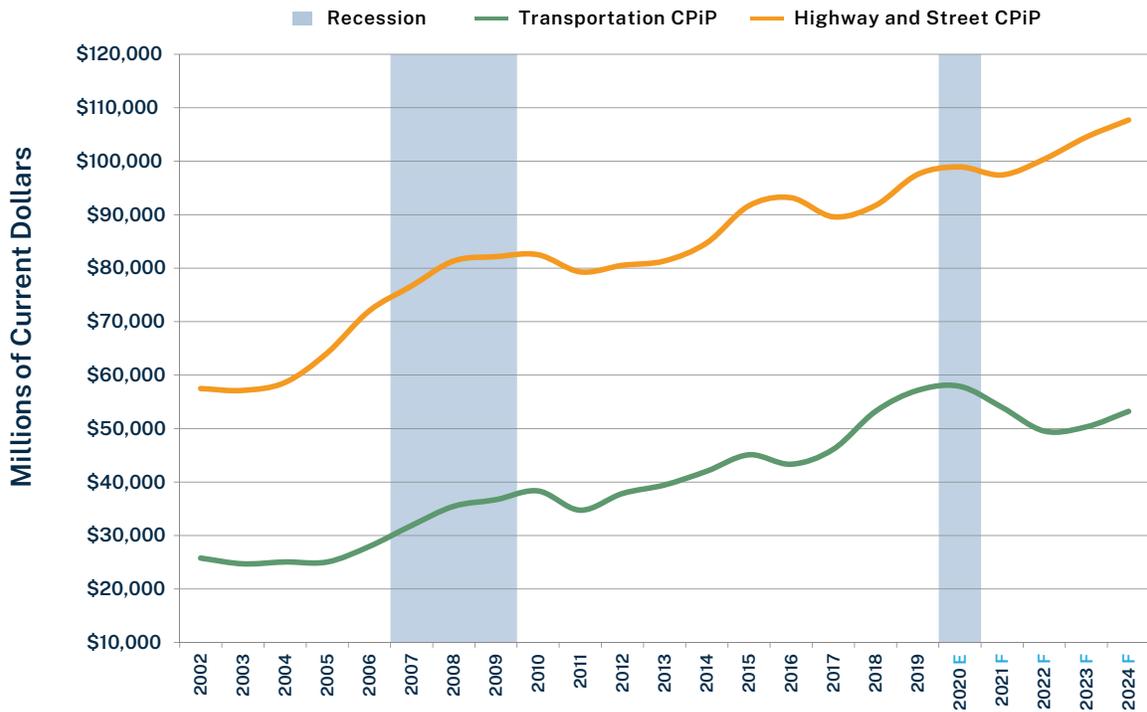


Backlogs are up and so are concerns

Civil construction firms continue adding to their backlogs and picking up new work, but there is growing concern for what 2021 and 2022 will bring, particularly for public construction markets. Most companies have seen a moderate to significant increase in competition, and 60% say bid prices are decreasing. This is not unexpected headed into a forecast construction decline, when we expect to see companies get more competitive and lower bid prices to build backlog as a cushion.

[According to the FMI Heavy Civil Construction Index](#), expectations for the second quarter of the year will reflect what happened in late 2020. Companies pursuing residential site development anticipate that market—a current shining star among all segments—to continue strong growth. Highway, bridge and other civil construction markets aren't likely to

Heavy Civil Transportation and Highway Street Construction Put in Place



show the same resilience, as contractors await clarity on the Fixing America’s Surface Transportation (FAST) Act renewal. Also, many have seen state and local programs reduced because of declining state and local tax receipts.

President Joe Biden’s administration has indicated investment in infrastructure is a priority, but there is still uncertainty around the ultimate outcome. The near-term outlook for state investment is similar since budgets continue to suffer, and increases in state and local spending on transportation and infrastructure remain to be realized in many areas.

Steps to take now

While the outlook for the rest of the year remains murky, there are some insights from our recent market research that heavy civil construction executives should review. For example, backlog book-

to-burn rates are growing, with 37% of companies increasing backlog at a faster rate. Concurrently, we’re seeing more competition on bids, while bid prices are dropping.

This may be a sign of companies competing aggressively to build backlog ahead of a downturn, or it may simply be companies building back after a year of accelerated schedules. Whether these trends continue for the remainder of 2021 is yet to be seen. But based on prior economic cycles, we can expect to see continued tightening if there isn’t a significant government stimulus, given our forecast for a downturn this year and next.

No matter what outcomes 2021 brings for the sector, there are several strategies all heavy civil contractors can use to take advantage of opportunities and continue to strengthen their market positions.



- **Build a solid diversification strategy.** Even in down markets, parts of the sector will continue to grow. We're tracking several areas (e.g., alternative energy infrastructure, warehousing and data centers) which may create opportunity for some heavy civil contractors. Be sure to scour market information to discover where opportunities will materialize, no matter what the competition is doing.
- **Avoid rash decisions.** As we learned during the last recession, quick reactions can lead to unforeseen problems. Many companies shifted from private site development, assuming the move to building highways or other infrastructure projects would be a natural alternative. Limited experience in these segments caused growing pains and losses.

It's OK to make these strategic decisions based on anecdotal evidence or intuition. Other times you need more facts or data to make those decisions or successfully implement new strategies. For example, examine the buying behaviors of customers within potential new markets and how they differ from your current markets. Although technical skills may be similar, adjacent markets often require different knowledge of customers, risk awareness or financial understanding. It's easy to recognize the difference between private

residential and public highway construction, but similar differences also exist between other segments. Understanding these distinctions is key to execution.

To avoid mistakes, take a pragmatic approach by asking yourself questions such as: What are the key differences between our current customers and our prospects? Which projects should we avoid? How aggressive are we going to be in pursuing work? How can we plan effectively now to avoid having to make uninformed decisions when challenges arise?

- **Rightsize and reassess equipment fleets.** For most heavy civil construction companies, the equipment fleet is the biggest asset on the balance sheet. The current market environment represents the textbook example of when companies should reassess equipment investments. This means you should consider not only the total investment, but also the ratio of lease versus own and the mix of the fleet as well. Focus on optimizing the performance of these assets by investing in management, processes and technology that increase productivity, usable time and the life of your equipment.

- **Be proactive with labor decisions.** If an economic decline or market shift occurs, the “people decisions” are always the most difficult ones. It’s natural to work hard to hold onto a talent base that was incredibly difficult to build. However, if you foresee an extended decline or changes in labor needs because of market shifts, it’s wise to act quickly. Conduct an objective assessment of permanent employees, including an assessment of their capabilities, their attitudes and their abilities to learn new skills. This helps you prepare for potential market shifts.
- **Differentiate yourself from the competition.** Our research shows that competition continues to increase for contractors in the heavy civil sector. Bid prices are declining, which means companies will have two choices. Option one is to drive costs down to win in a more competitive bid market. This is typically done through a relentless focus on operational excellence and consistent processes. The second option is to be more selective in the work you pursue and only consider those projects that match your distinct capabilities. If you don’t have a clear strategy to win (i.e., specialized equipment, proximity, experienced team or something else), consider passing on the opportunity. For opportunities where price is only one factor, prior investments in technology, processes, experience, customer knowledge and other differentiators will be key. Not every opportunity will afford you the chance to differentiate, so focus your resources wisely.
- **Avoid panic bidding.** Firms need to balance backlog maintenance with bids that are too low and unprofitable. Defining and committing to a disciplined approach to bidding will help you avoid chasing projects outside your areas of expertise or panic bidding on projects. Most contractors claim to have go/no-go processes, standardized project kick-offs and productivity evaluation processes, etc. However, we find many do not follow those processes consistently, haven’t trained newer hires on these fine points, or rely on outdated processes. These inconsistencies, combined with pressures on estimators to “win work,” create an environment that can lead to inconsistent bid day results. We encourage you to work now to refresh and retrain on project pursuit processes and strategies.

Being prepared

As 2021 continues, contractors need to pay attention to market shifts. Whether they’re diversifying, selling equipment, downsizing labor or exploring new market opportunities, smart contractors will carefully evaluate their businesses and strategic goals when making these decisions.

No matter what the rest of the year brings, now is the time to reevaluate market strategies and make plans or adjustments to ensure continued profitability. Continual innovation is critical, particularly when that innovation either strengthens current capabilities or helps companies meet critical demand in target markets or geographies.

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