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|-------|---------|------------|---------------|-------------|----------|------------|----------------|
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## **ARCHITECTURE AND ENGINEERING: PREPARING FOR INDUSTRY RECOVERY**

By Vic Hausmaninger, CPA, CEO, HBLA CPAs

HBLA, an Irvine-based CPA firm, works with our clients on a proactive basis to assist them with timely responses to industry changes. We continually monitor industry, economic and tax developments. We evaluate these developments and then assist our clients to make necessary changes—before things happen. For example, in 2008, before the word “recession” was used by the media, we issued a “white paper” entitled *Preparing for the Recession Of 2008*. Those clients that followed the recommendations were able to “weather the storm reasonably well. Our focus now is to assist clients in positioning themselves to take advantage of the anticipated improvements in the economy in 2012.

### **Industry Review of Last Few Years—**

Currently the industry consists of approximately 98,000 architecture and 139,000 engineering businesses nationally of which 20% are located in the West (15% in California). Total revenues approximate \$40 billion and \$177 billion, respectively, of which 22% are in the West (17% in California). Before the recession, the industries experienced relatively strong growth with revenues rising 5-10% annually in the mid-2000s through 2007-2008 after which demand conditions deteriorated significantly. The strong growth was largely driven by rising values of construction activities that experienced double digit growth in those years. Beginning with 2008, revenues began a rapid decline with annual revenues dropping rapidly with the worst decline in 2009 (15%) when long term contracts, started earlier, began running out. Of course, profit margins suffered in the same manner leading to cost cutting measures in 2009-2010 to mitigate losses including major reductions in employees, the largest cost component. Unfortunately, many small operators (particularly those serving the residential markets) were forced to close their doors.

### **Industry Outlook for 2011 and Beyond—**

Industry reports and forecasts indicate that over the next five years there will be a return to growth as the economy and construction markets gradually recover with average annualized revenues expected to increase about 4% from the 2009 trough--mostly in the non-residential market which makes up the biggest component of revenues. Residential construction is also expected to increase but at a very slow level with only approximately 800,000 units expected for 2012. Overall, even though growth is expected for the next five years, a return to the levels experienced in the mid 2000s is not expected until 2016 or after. And, clearly, this slow turn around can be adversely effected by consumer

sentiment, economic conditions, interest rates, and ability of investors and businesses to obtain credit.

### **Preparing for Future Growth—**

Even though uncertainties still exist with respect to future economic stimulus programs, tax strategies, and investor and business sentiment, firms need to be prepared to maximize the growth opportunities when they arise. Some general future key success factors to consider include:

- Having a clear market position -- have a clear definition of general and, especially, niche areas of expertise and a reputation in certain areas of architecture and engineering;
- Ability to compete on tender -- since many projects are tendered, to be able to compete for tenders for work, as well as generate on-going and repeat, non-tendered work, which may be less price sensitive;
- Ability to quickly adopt new technologies -- to be able to offer clients the latest in technology using computerized models, if required;
- Effective cost controls -- to establish effective cost controls over all project work, particularly for direct labor input and any sub-contract work;
- Willingness to outsource when appropriate -- to have strategic alliances with a number of specialist building and construction-related services firms to outsource any highly specialized areas.

• Availability of working capital -- to have access to financing for growth in accounts receivable and contracts in process and to know how much financing will be needed through preparation of detailed operating and cash flow forecasts.

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