

SUCCEEDING IN A DIFFICULT MARKET

Presented by

Mark W. Bridgers
Consultant
FMI Corp.

WORLD TRADE CENTER DISASTER, DEBRIS REMOVAL, INSPECTION & DISPOSAL

Presented by

Ben R. Turner
President and CEO
Phillips & Jordan, Inc.

The year 2001 was one of dramatic movement for insurance and surety bond markets. Premiums for many contractors and owners are up 70 percent or more, and markets for some specialty coverages that were readily available 5 years ago have all but evaporated. In this general session, an experienced construction risk and insurance consultant will outline the general impact of current insurance conditions on the financial performance of contractors and, in turn, on owners' 2003 construction costs. Find out what is expected to happen in the next 12 months and what you can do to protect your company's interests. Subsequently, the COO of a general and specialty contractor will share his insights into their experience in the World Trade Center cleanup operations.

Tuesday, November 12, 2002

Mark W. Bridgers
Consultant
FMI Corporation

Mr. Bridgers is a keynote speaker presenting the first half of Tuesday's General Session, "Succeeding in a Difficult Market." He is a consultant with FMI, management consultants to the construction industry. He works with owners or purchasers of construction contracting services in the areas of organizational analysis, construction cost management, accounting and financial issues, and strategy development. His clients include retail firms, manufacturing firms, national developers and property managers, and public owners. Mr. Bridgers works closely with these clients' managers of engineering and/or construction. Typical projects include analysis of an organization's financial performance; development and implementation of tools to reduce construction cost, life-cycle cost, and operational friction; restructuring of organizational processes and procedures; and leadership development.

Mr. Bridgers brings more than 5 years of financial engineering, surety bonding, and reinsurance experience to FMI. His in-depth knowledge of owner concerns, financial topics, and the surety and reinsurance markets—combined with his ability to convey difficult construction, insurance, and financial topics to laypeople and professionals alike—make him an enthusiastic and exciting speaker. He has spoken at owner-group meetings, construction associations, surety gatherings, and professional meetings nationwide. Mr. Bridgers also delivers FMI's Job Profits, Pricing & Bidding, and Financial Management for Non-Financial Managers programs.

Mr. Bridgers holds a master's degree in business administration from the University of Virginia's Darden School and a bachelor's degree in financial management from Clemson University. He has earned the titles of Chartered Property & Casualty Underwriter (CPCU) and Associate in Reinsurance (Are).

Ben R. Turner
President
Phillips and Jordan, Inc.

Mr. Turner is a keynote speaker for the second half of Tuesday's General Session: "World Trade Center Disaster, Debris Removal, Inspection & Disposal." He has been with Phillips and Jordan since 1977. In that time he has held the following positions: Project Manager (1977-1978), Vice President (1978-1983), Vice President and Florida Operations Manager (1983-1989), Executive Vice President and Chief Operating Officer (1989-1993), and President (1993-present). As President Mr. Turner is responsible for all Phillips and Jordan projects and personnel.

Past projects include numerous projects for Disney in Orlando, Florida; dams and reservoirs throughout the Southeast; powerline clearing in the Everglades; pipeline clearing in New York, Maine, and Missouri; landfill and liner projects; disaster recovery efforts including Hurricanes Andrew, Fran, Bonnie, Irene, Hugo, and Opal; golf courses in South Carolina, Alabama, Indiana, and Florida; reclamation projects for the phosphate mining industry; various manufacturing, commercial, and power plant sites; community developments; airports in Florida and North Carolina; and highway construction in the Southeast.

Mr. Turner was Phillips and Jordan's Operations Manager for the Hurricane Andrew and Hurricane Fran recovery missions and the MCCC Mine disaster, as well as the World Trade Center Mission.

Before coming to Phillips and Jordan, Mr. Turner was Company Manager for the Fred Lothridge Company, a civil works contractor in Gainesville, Georgia.

SUCCEEDING IN A DIFFICULT MARKET

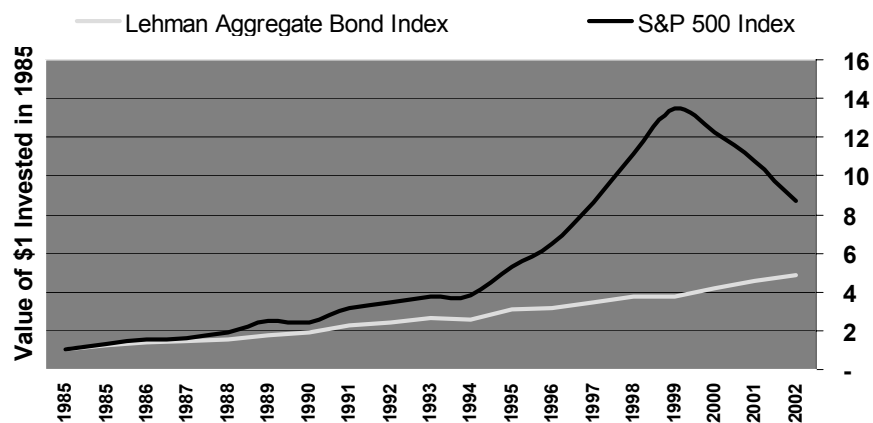
Mark W. Bridgers
FMI Corp.

Objectives

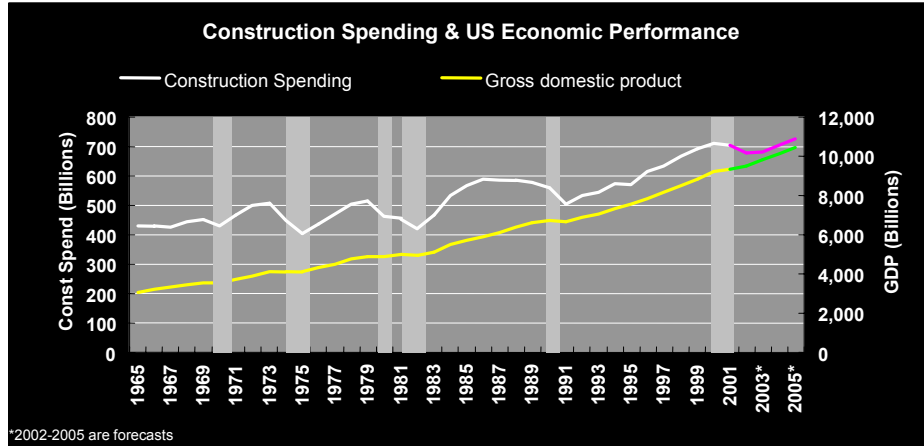
- Understand macro environment in which we currently operate.
- Introduce major risk factors that I see for contractors and owners.
- Tell you what I would do about them - short-term and long-term.

Macro Environment (1 of 7)

15 Year Equity & Bond Returns

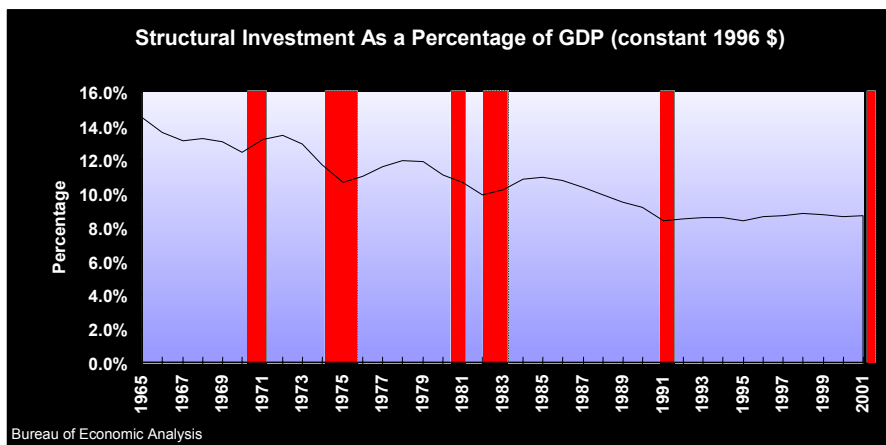


Macro Environment (2 of 7)



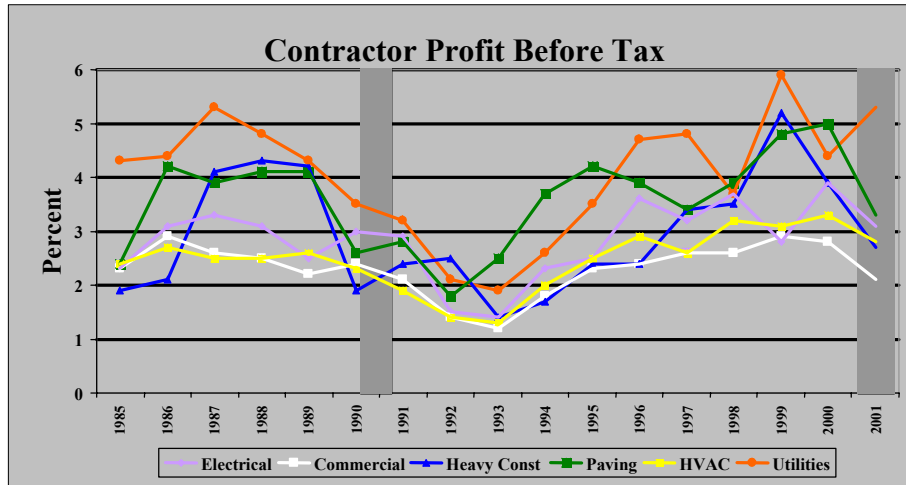
Recession Periods Are Shaded Lighter Gray

Macro Environment (3 of 7)



Recession Periods Are Shaded Darker Gray

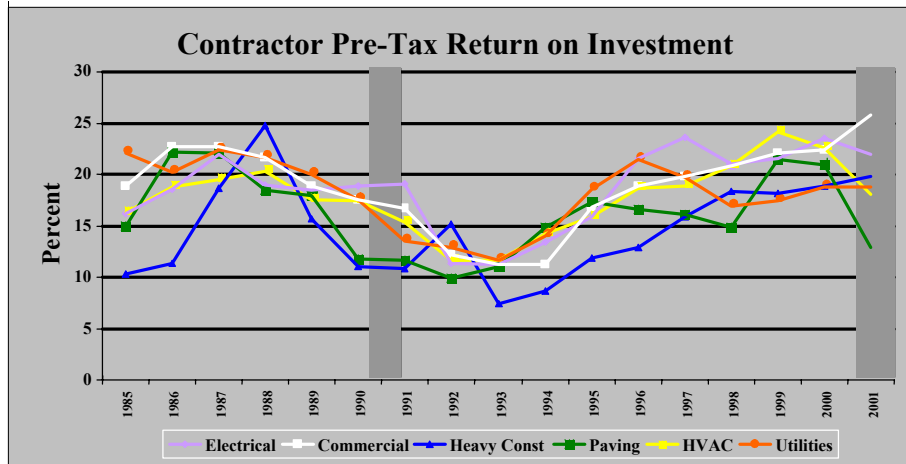
Macro Environment (4 of 7)



Risk Management Associates, Annual Statement Studies, 1985-2001

Recession Periods Are Shaded Darker Gray

Macro Environment (5 of 7)

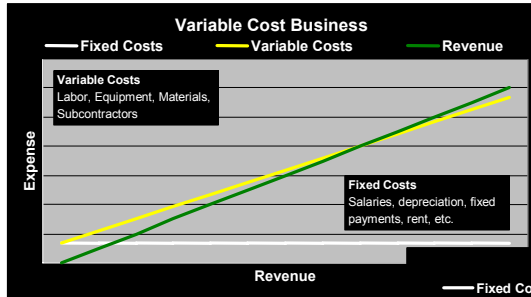


Risk Management Associates, Annual Statement Studies, 1985-2001

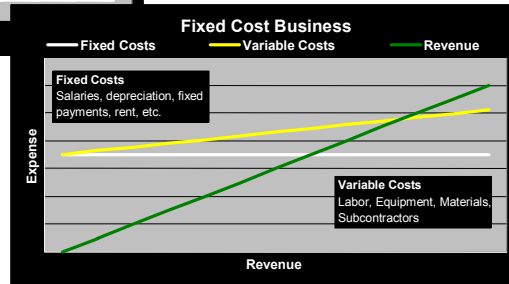
Recession Periods Are Shaded Darker Gray

Macro Environment (6 of 7)

Variable Cost Business

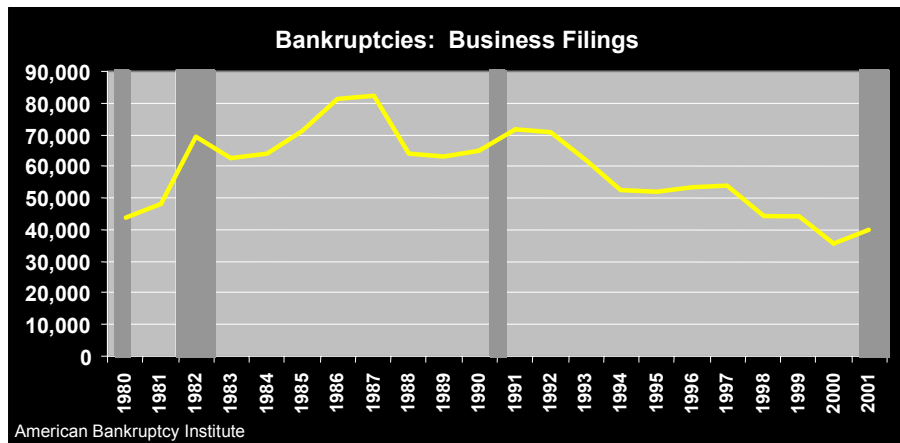


Fixed Cost Business

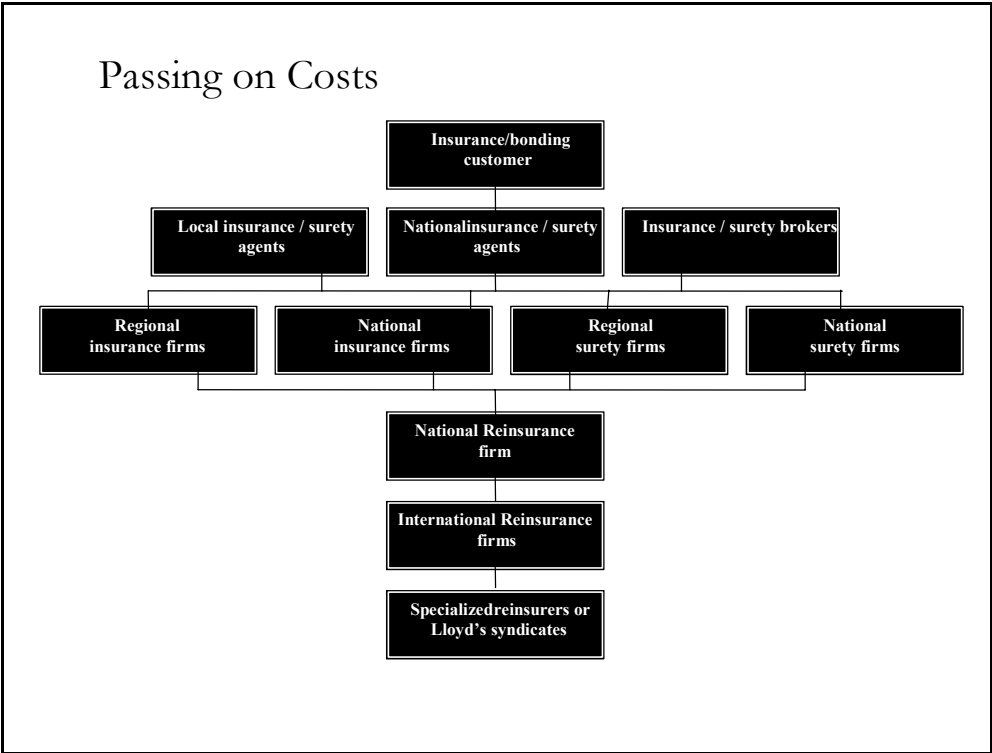


Volume Kills –
Profit Thrills!

Macro Environment (7 of 7)



Recession Periods Are Shaded
Darker Gray



Tiered Structure

- The pricing of insurance and bonds is a function of the cost of reinsurance. As the cost of reinsurance rises, so will eventually the cost of insurance/bonds.

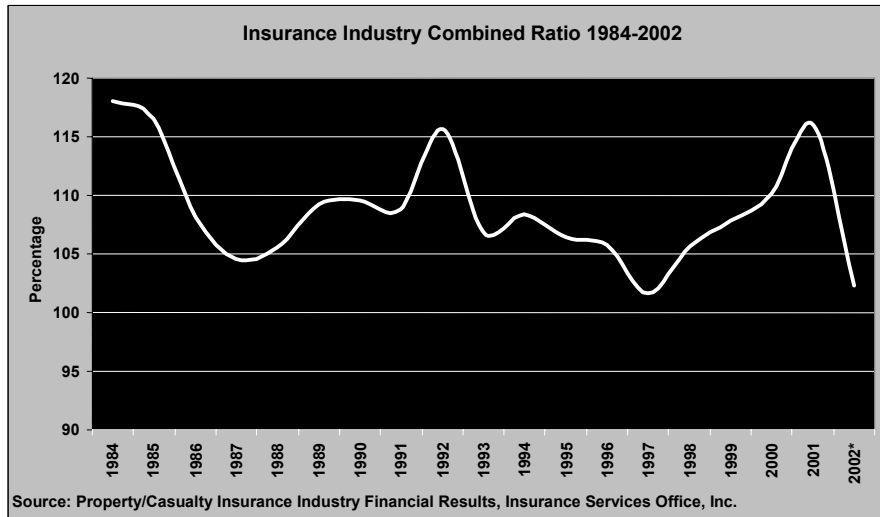
Discouraging Results - Insurance *(1 of 3)*

- Property and Casualty ... 2001 was the industry's worst year ever.
 - 2001 - First ever year-end net loss of \$7.3 billion.
 - 2001 - \$18 billion in unrealized losses due to both equity and bond performance.
 - 2001 - Decline in surplus of 8.6%
 - Three of the industry's top 10 largest catastrophes.
 - 2001 - Combined ratio of 116%.

Discouraging Results - Insurance *(3 of 3)*

- Results - Insurance
 - Insurance covers are all increasing in price
 - Greater difficulty getting certain coverages
 - If coverage is available, getting adequate limits difficult.

Property & Casualty Industry Results



Property & Casualty Industry Results

Largest US Catastrophic Losses – 1985 to 2001

Date	Event	Insured loss * (000,000)
9/11/2001	Terrorist attack on WTC, Pentagon, etc.	19,000
6/5/2001	Tropical storm Allison; rain, floods	3,150
4/6/2001	Hail, floods, and tornados	1,900
9/10/1999	Hurricane Floyd; heavy downpours, flooding	2,508
5/3/1999	Series of over 70 tornados in the Midwest	1,578
9/20/1998	Hurricane Georges	3,833
5/15/1998	Wind, hail, and tornados (MN, IA)	1,461
1/5/1998	Cold spell with ice and snow	1,337
9/5/1996	Hurricane Fran	1,806
10/1/1995	Hurricane Opal	2,440
9/14/1995	Hurricane Marilyn	921 C
5/5/1995	Wind, hail, and flooding (TX, NM)	1,319
1/17/1994	Northridge earthquake	16,720
1/17/1994	Freezing weather and snowstorms hit east coast	850 D
10/27/1993	Forest fires which spread to urban areas (CA)	1,133 A
3/10/1993	Blizzard, tornados	2,144
11/12/1992	Rain, snowstorm, floods	1,228 A
9/11/1992	Hurricane Iniki	2,019
8/23/1992	Hurricane Andrew	20,185
4/29/1992	Race riots in Los Angeles	886 C
4/28/1992	Storm, hail, tornados in OK and TX	852 D
10/29/1991	Hurricane Grace	1,300
10/20/1991	Forest fires spread to urban areas, drought	1,560
2/16/1991	Hurricane Bob	1,006 B
10/23/1989	Explosion in petrochemicals plant	1,892
10/17/1989	Loma Prieta earthquake	1,428
9/15/1989	Hurricane Hugo	5,990

Source: Swiss Re, SIGMA, Natural catastrophies and man-made disasters - 1995, 1996, 1997, 1998, 1999, 2000, and 2001.

* Excludes liability loss and indexed to 2001

A = Includes loss development through 2000 and indexed to 2000.

B = Includes loss development through 1998 and indexed to 1998.

C = Includes loss development through 1997 and indexed to 1997.

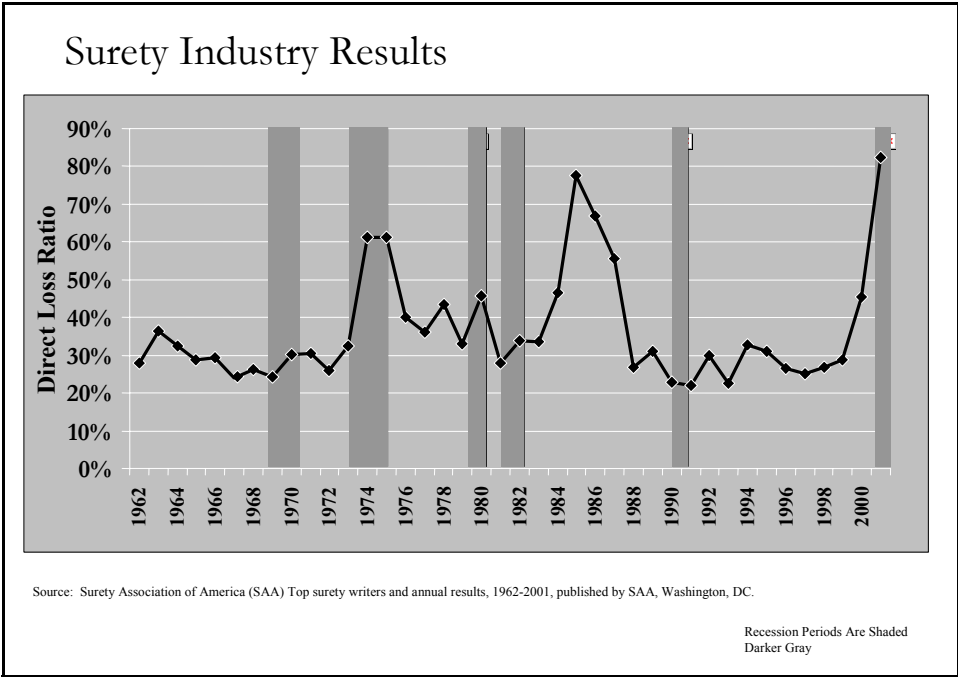
D = Includes loss development through 1996 and indexed to 1996.

Tightening Surety Industry *(1 of 2)*

- Surety Underwriting
 - General looseness in surety underwriting since 1992.
 - Proliferation of new firms offering bonding between 1990 & 2000. (This is currently reversing)
 - Large national firms very focused on maintaining or growing market share between 1992 - 2001.
 - Consolidation and concentration of bond premium with top 10 firms.
 - Now What?

Tightening Surety Industry *(2 of 2)*

- 2000: 20 surety losses in excess of \$40MM, 8 of these were greater than \$80MM.
- 2001: Continued deterioration producing the highest direct loss ratio, 82.3, on record
- 2002: Major (potential) commercial bond losses through Enron. Petrobras.
- Commercial surety driving the results - both premium growth & losses from 1996 to present.



Top Ten Surety 1990

Top 100 Surety Writers - 1990			
Company Name	Direct Written Premium	% of Total	Direct Loss Ratio
1 Fidelity & Deposit Group	137,602,649	6.4%	12.10%
2 United States Fidelity & Guarantee Company	121,763,169	5.7%	19.73%
3 Reliance Group	120,842,306	5.6%	25.63%
4 The Aetna Live & Casualty Group	114,611,650	5.3%	93.49%
5 Fireman's Fund	96,258,065	4.5%	29.27%
6 Seaboard Surety Company	93,186,013	4.3%	-23.87%
7 Continental Insurance Company	93,164,965	4.3%	25.31%
8 CNA Group	83,368,359	3.9%	35.94%
9 Safeco Insurance Group	74,346,384	3.5%	5.55%
10 Hartford Ins Group	70,584,624	3.3%	30.75%
Sum of Top 10	1,005,728,184	46.7%	26.75%
All others Various	1,148,592,878	53.3%	19.57%
Totals	2,154,321,062	100.0%	22.93%

Source: Surety Association of America (SAA) Top surety writers and annual results, 1962-2001, published by SAA, Washington, DC.

Top Ten Surety 2000

Top 100 Surety Writers - 2000

Company Name	Direct Written Premium	% of Total	Direct Loss Ratio	Net Loss Ratio
1 Travelers Property Casualty Corporation	388,872,000	11.5%	27.2%	19.6%
2 The St. Paul Companies	387,649,000	11.5%	53.8%	25.7%
3 CNA Surety Corporation	285,528,000	8.4%	7.0%	-4.8%
4 Zurich Group	206,922,000	6.1%	36.4%	25.2%
5 American International Group	160,025,000	4.7%	108.1%	37.6%
6 Liberty Mutual Group	141,603,000	4.2%	51.8%	14.5%
7 Ace USA Group	125,781,000	3.7%	69.8%	74.7%
8 Safeco Insurance Companies	124,739,000	3.7%	44.4%	30.6%
9 Chubb Group of Insurance Companies	120,138,000	3.6%	60.5%	20.2%
10 Fireman's Fund Insurance Companies	106,144,000	3.1%	33.7%	35.3%
Sum of Top 10	2,047,401,000	60.5%	43.9%	23.7%
All other: Various	1,335,361,000	39.5%	43.0%	32.1%
Totals	3,382,762,000	100.0%	43.5%	26.8%

Source: Surety Association of America (SAA) Top surety writers and annual results, 1962-2001, published by SAA, Washington, DC.

Top Ten Surety 2001

Top 100 Surety Writers - 2001

Company Name	Direct Written Premium	% of Total	Direct Loss Ratio	Net Loss Ratio
1 Travelers Property Casualty Corporation	446,066,804	13%	69.1%	46.8%
2 The St. Paul Companies	375,647,862	11%	56.8%	45.0%
3 CNA Surety Corporation	304,892,266	9%	87.4%	53.0%
4 Zurich Group	268,616,668	8%	43.3%	37.9%
5 American International Group	185,914,009	5%	144.6%	143.3%
6 Safeco Insurance Companies	153,684,018	4%	60.2%	29.1%
7 Liberty Mutual Group	145,033,694	4%	165.8%	64.6%
8 Chubb Group of Insurance Companies	136,293,956	4%	291.7%	203.9%
9 Fireman's Fund Insurance Companies	117,854,491	3%	252.6%	82.7%
10 The Hartford Insurance Group	115,471,829	3%	60.4%	30.0%
Sum of Top 10	2,249,475,597	65%	103.9%	68.0%
All others	1,195,804,727	35%	41.2%	32.1%
Totals	3,445,280,324	100%	82.3%	56.2%

Source: Surety Association of America (SAA) Top surety writers and annual results, 1962-2001, published by SAA, Washington, DC.

Surety Reinsurer Performance (*Estimates*)

<i>Year</i>	<i>Premiums Earned (000's)</i>	<i>Reinsurance Losses (000's)</i>	<i>Loss Ratio</i>
1997	\$228,000	(\$120,000)	53%
1998	\$296,000	(\$157,000)	53%
1999	\$237,000	(\$225,000)	95%
2000	\$409,000	(\$666,000)	163%
2001	\$515,000	(\$1,157,000)	225%

Source: Surety Association of America (SAA) Top surety writers and annual results, 1997-2001, published by SAA, Washington, DC.

Tightening Surety Industry

- Results - Surety (Commercial & Contract)
 - Greater financial scrutiny.
 - Restriction in bond size.
 - Restriction in accumulated bond exposure.
 - Large or international projects will face capacity issues.
 - Surety Reinsurance coverage unavailable for some large contractors.

Surety Consolidation or Elimination

- Consolidation
 - Fireman's Fund into St. Paul
 - USF&G into St. Paul
 - Aetna into Travelers
 - Reliance into Travelers
 - Western Surety into CNA
 - American States into Safeco
 - Washington International into NAS/Swiss Re
- Elimination
 - Amwest
 - Frontier
 - Meadowbrook
 - Nobel
 - American Bankers Ins.
 - Ranger Insurance Co.

Future of the Surety Industry?

- Continued focus on market share by large firms?
Why?
- Continued focus on consolidation.
- Smaller/Regional sureties focused on profitability, financial control.
- Contractor bankruptcies expected to increase through 2002 & 2003.

Design/Build - Special Concerns *(1 of 4)*

- Divide the approach to a project into three categories:
 - How the job will be managed - GC, CM@Risk, CM Agency
 - How the price will be determined - hard bid, select bid, negotiated
 - How the job will be constructed - design/bid/build, contractor led design/build, architect led design/build, etc.

Design/Build - Special Concerns *(2 of 4)*

- Owners who use design/build firms face special challenges
 - How to ensure we get the facility we expected?
 - How do we ensure the firm providing design services is adequately protected by E&O coverage.
 - How do we select a firm to provide both design and construction services.
- These specialty covers are much more expensive or in some instances, not available.

Design/Build - Special Concerns *(3 of 4)*

- Contractors used to lead design/build
 - Lack of experience with design/build approach
 - Tend not to purchase appropriate coverage
 - Select inadequate limits
 - Choose a financially unstable insurer
- A surety bond is not adequate protection of the owners interests in the event of design errors.

Design/Build - Special Concerns *(4 of 4)*

- Architects used to lead design/build
 - Lack of experience with design/build approach
 - Construction management/leadership experience
 - Inability to provide a surety bond
 - Financial resources in the event of disputes or conflict
 - Lack of familiarity with local labor market

Conclusions *(1 of 2)*

- Increasing cost of insurance/surety will punish financially unstable contractors.
- Unavailability or under insurance of risks both by contractors and owners.
- Greater risk placed on owners to do their homework when selecting a contractor.

Conclusions *(2 of 2)*

- Economy will limit capital expenditures by owners increasing competition among contractors.
- Continued bankruptcies and economic fall out for contractors through 2002 & 2003.
- The worst is likely still in front of us.

What Should A Contractor Do? *(1 of 4)*

- Risk Control
 - Candid conversation with agent/broker - where are policies or bonds placed and how are firms performing?
 - Obtain debt rating and A.M. Best's reports on companies where your policies reside.
 - Define the options, approaches, and firms that may help control potential property/casualty premiums.
 - Meet with your property/casualty/bond underwriter and discuss how their firm is responding to insurance industry challenges.

What Should A Contractor Do? *(2 of 4)*

- Proactive Management/Leadership
 - Take an objective look at your financial performance and determine the amount of surety credit you “really” need.
 - Take an objective look at your cash flow and revenue projections and determine the amount of bank credit you need - keep some power dry!
 - Speak with your surety agent/broker to discuss various underwriting requirements that sureties are implementing.

What Should A Contractor Do? *(3 of 4)*

- Strategic & Business Planning (with Budgeting)
 - Prepare a legitimate strategic plan describing the direction of your firm over 3-5 year horizon.
 - Prepare a legitimate business plan outlining your approach to leading and managing your firm over the next 12-24 months.
 - Build a legitimate and detail budget with “what if” scenarios of best, expected, and worst case.
 - Discuss with your agent/broker/CPA how to present this information to your surety or bank.

What Should A Contractor Do? *(4 of 4)*

- Maintain Flexibility
 - Make your business the right size for your market and economic conditions! (Volume Kills, Profit Thrills)
 - Be ready for the unexpected.

What Should Owners Do? *(1 of 3)*

- Risk Control
 - Find out who your contractors' policy/bond coverage is with and how well are the firms performing.
 - Obtain debt rating and A.M. Best's reports on companies where your and your contractors policies reside.
 - Be prepared to understand the change in your risk profile due to contractors who have implemented innovative solutions to control insurance costs.

What Should Owners Do? *(2 of 3)*

- Surety/Bond Use
 - Consider the use of bid, performance, and payment bonds as a screening mechanism to eliminate unqualified contractors.

What Should Owners Do? *(3 of 3)*

- Proactive Management/Leadership
 - Request copies of your contractor and key subcontractor financial statements and learn to “read” these documents.
 - Add additional characteristics other than price into your contractor solution criteria.
 - Understand coverage requirements necessary for adequate protection when using design/build.

Some Tools for Contractors *(1 of 3)*

- AM Best’s - <http://www.ambest.com/homepage.asp>
- Company Rating Information - <http://www3.ambest.com/ratings/>
- Surety Association of America - <http://www.surety.org>
- Surety Information Office - <http://www.sio.org/>

Some Tools for Contractors (2 of 3)

Strategic Planning Process

A	B	C	D	E	F
SWOT	Mission	Goals and Objectives	Strategies	Action Plans	Additional Planning
Define Value Chain	State Overall Aim	Explore Possible Goals	Brainstorm Strategy Options for Goals	Draft Tasks to Implement Strategy	Forecast Financial Results
Identify Internal Strengths, Weaknesses	Define Target Markets	Select 3-5 Key Goals	Evaluate Strategic Options	Draft Tasks for Strategy Reinforce.	Forecast Capital Requirements
Define Core Competency(ies)	Identify Principal Services	Identify 1-2 Key Measures Per Goal	Consider Functional Strategies	Evaluate Resource Requirements	Forecast Personnel Requirements
Analyze Market	Define Geographic Domain	Verify Info Suppt. For Measures	Select 1-2 Strategies Per Goal	Finalize Tasks	
Determ. Competitive Positioning	State Corporate Values			Assign Task Leader	
Identify External Opportunities, Threats				Schedule Implementation	

Some Tools for Contractors (2 of 3)

Business Planning Process

- Business Definition
- Financial and Accounting Plans
- Work Acquisition Strategy
- Performance Capacity
- Action Plans & Management Controls

Some Tools for Contractors (3 of 3)

<i>Strategic Planning</i>	<i>Business Planning</i>
Process oriented	Product oriented
Use to change business focus	Used to improve performance within existing areas
Longer horizon (3-5 years)	Short or medium time horizon (2 or less years)
Never finished – only current versions exist	Completed for a set planning period
Emphasis on corporate vision, values and mission	Emphasis on facts and projections
Strategy oriented	Tactically oriented
Objective is to shape corporate culture	Corporate culture shapes business plans

Some Tools for Owners (1 of 3)

- AM Best's - <http://www.ambest.com/homepage.asp>
- Company Rating Information - <http://www3.ambest.com/ratings/>
- Surety Association of America - <http://www.surety.org>
- Surety Information Office - <http://www.sio.org/>

Some Tools for Owners (2 of 3)

FMI's Contract Type/Pricing Decision Matrix					
Characteristics	Hard Bid (Lump Sum, LS + Savings)		Select Bid (Lump Sum, LS + Savings)		Negotiate (GMP, T&M, LS + Savings, Cost +)
	Owner repetitive construction	High Repetition	3	2	1 or Mitigate
Owner experience with construction	High	3	2	1 or Mitigate	Low
Owner risk tolerance	High	3	2	1	Low
Technical construction complexity	Low	3	2	1	High
Construction coordination complexity	Low	3	2	1	High
Owner management staff	Adequate	3	2	1 or Mitigate	Limited
Relative owner project work load*	Low	3	2	1	High
Scheduled speed	Reasonable	3	2	1	Fast Track
Owner geographic familiarity	High	3	2	1 or Mitigate	Low
Site / building condition	Clean / prepared	3	2	1	As-is, difficult
Owner culture	Hard nosed Adversarial	3	2	1	Relationship, team oriented

* Relative to experience of general contractor, construction manager, and owner.

Some Tools for Owners (3 of 3)

FMI's Owner Decision Matrix					
Characteristics	Project Management Process			Management Service	
	General Construction	Construction Management at Risk	Construction Management Agency		
Project Budget	Very Tight	1	2	3	More Flexible
Relative Project Size*	Small	1	2	3	Large
Owner Repetitive Construction	High Repetition	1	2	3	Low Repetition
Owner Experience with Construction	High	1	2	3	Low
Owner risk tolerance	High	1	2	3	Low
Relative Project Duration*	Short	1	2	3	Long
Technical construction complexity	Low	1	2	3	High
Construction coordination complexity	Low	1	2	3	High
Owner management staff	Adequate	1	2	3	Limited
Relative owner project work load*	Low	1	2	3	High
Scheduled speed	Reasonable	1	2	3	Fast Track
Owner geographic familiarity	High	1	2	3	Low

* Relative to experience of general contractor, construction manager, and owner.