

Private Equity's Power Play

As Investors Flood the Engineering Sector, Valuations Rise and Firms Become More Strategic and Business-Oriented—But Not Without Potential Risks

BY BETH BRAVERMAN



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Amid a booming industry, engineering firms—like many professional services companies—have still faced growing succession challenges and increased consolidation over the past decade. At the same time, private equity (PE) investment has grown significantly, creating additional options for firm ownership and capitalization, while also impacting valuations and merger and acquisition strategies.

PE's interest in the industry reflects many factors, including a recognition of the government's Infrastructure Investment and Jobs Act, which has brought billions of dollars to fund projects across the United States.

"Nothing gets the attention of investors like a multiyear, multibillion-dollar spending program by the federal government, because you can plan and execute long-term strategy around it," says Nick Belitz, principal of advisory services at Morrissey Goodale.

PE firms also see engineering businesses as an opportunity for them to diversify their portfolios.

"PE firms are looking for alternative investments," says Brendon Cussio, principal of mergers and acquisitions advisory and the sell-side practice at Morrissey Goodale. "Historically, they like businesses with physical, tangible assets. With professional services, the assets are the people. It's a different model, but they've found it to be successful, assuming the proper alignment of incentives."

U.S. acquisitions made by PE firms have increased from 12 percent in 2016 to 39 percent in 2023, according to Morrissey Goodale. Over that period, the percentage of *Engineering News-Record* Top 100 firms backed by PE shot up fivefold, from 4 percent to 22 percent.



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PRINCIPAL
MORRISSEY GOODALE

GROWING WITHOUT PRIVATE EQUITY

As an alternative to private equity (PE), DeSimone Consulting Engineering has been focused on organic growth and mergers and acquisitions. It has added five businesses in the past four years, with another deal closing this month and three others in the works, primarily funding those acquisitions with free cash flow.

Atwell has taken a similar approach, says CEO Brian Wenzel, growing organically from a \$29 million company in 2010 to a projected \$480 million company with more than 1,800 employees. Much of that growth has been through acquisitions funded via debt or cash flow put back into the business. The firm has found that some acquisition targets are interested in a deal because Atwell *isn't* PE.

"We can talk very holistically about the approach to the organization in a way that doesn't make people feel like they're getting on a roller coaster," Wenzel says. "The strategy helps potential acquisitions understand our stability and their opportunities for growth. Atwell is a place where our acquired firms and new employees can learn, grow, and build a career that they're passionate about—while contributing to the direction of the larger organization."

That approach can also appeal to senior leaders within those organizations, including those who aren't interested in becoming owners.

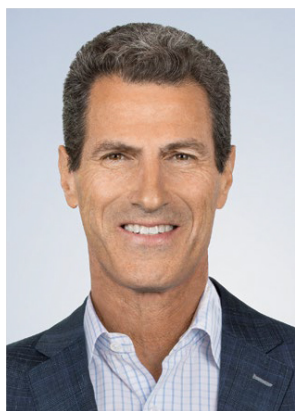
"We have shown them a path to continue to financial success with a focus on personal satisfaction, professional development, and financial reward. Our team members can do very well without necessarily having an equity interest in the company," says Atwell President Matthew C. Bissett.



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DARIN ANDERSON
CHAIRMAN AND CEO
SALAS O'BRIEN

RISING VALUATIONS

That increased investment has driven up valuations throughout the industry, says Ernesto Aguilar, CEO of PE-backed Ardurra, which has experienced rapid growth via acquisition in recent years.

“Part of the increase in valuations is because there was a big gap between private valuations and publicly traded companies,” Aguilar says. “Right now, when a deal comes up from a broker, they get 30 or 40 offers. If a big company comes up, they’re getting massive offers. It’s a sellers’ market. They get 15 to 25 offers.”

To avoid bidding wars, Aguilar says his company prefers to do its own sourcing for potential deals.

Supporters of PE-backed engineering firms believe that such financing can solve the succession challenges that have arisen as the next generation of engineers faces more economic hurdles and different priorities than their older peers, making them less able or less interested in purchasing their companies. Plus, there simply aren’t enough young engineers to replace all of the retiring baby boomer owners.



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“Ownership transition is something that has become challenging to do internally,” Cussio says. “Fewer minority owners have an appetite to borrow significant capital to buy out an exiting shareholder and take on the business risk. In general, the PE philosophy of holding an investment for a relatively short period of time and realizing a significant return on their invested capital in a similar period is also attractive to owners who are rolling equity as a part of a transaction with a PE partner. Additionally, access to growth capital helps firms grow faster than they can on their own.”

For example, a firm with a PE investment can immediately expand to new geographies, add new services, or hire more people, even in a tight labor market.

PROFESSIONALIZING THE BUSINESS

Proponents stress that PE firms can help professionalize engineering businesses, which are often run by teams with strong engineering backgrounds but less experience in finance or operations.

At Ardurra, Aguilar says that the company’s PE backer, Littlejohn & Co., has helped its back office keep up with the company’s rapid growth. For example, the PE firm has assisted with project management to integrate multiple enterprise resource planning platforms and helped recruit a new CFO and COO.

“One of the reasons we picked Littlejohn was that they understand it’s a people business, and we have to keep our people,” Aguilar says.

Darin Anderson, chairman and CEO at Salas O’Brien, says his firm has had a great experience since taking PE capital. The company first accepted a small investment from Caltius Structured Capital in 2020, and then a larger investment in January of this year from Blackstone. The firm remains supermajority employee-owned.

Anderson says that for more than a decade before the investment, Salas O’Brien had been averaging a 90 percent return on investment on its shares but saw the additional capital as an opportunity to continue growing while also taking some chips off the table for employee owners.

“We wanted anyone owning shares to be able to sell shares not only at the end of their career at retirement but whenever they needed liquidity, such as when their kids went to college or to buy a new house,” Anderson says. “More importantly, Blackstone, as a

world-leading asset manager, has been able to put us in contact with like-minded organizations to help us grow our business further.”

POTENTIAL DRAWBACKS

Like engineering companies, all PE firms are different, and some partnerships don't pan out as well as others. If a PE firm doesn't have a lot of experience in the engineering industry and doesn't understand how critical the human capital element is to success, that could create challenges for a firm concerned about finding the right partner, Cussio says.

And sometimes the introduction of PE can be a culture shock for a traditional engineering firm. Firms accepting PE capital should have PE representatives sitting on their board and asking difficult questions.



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ARDURRA

“It can be uncomfortable because there are new voices asking new questions about the business in board meetings,” Belitz says. “And that dynamic can be problematic for leaders who aren't used to it. It can be a good thing in the long run, but it changes the way that people think about and run their businesses.”

Given the potential drawbacks, not everyone feels that PE is the best path for most engineering firms.

“I believe that privately held firms, over the course of the next several years, will enjoy a significant advantage in the marketplace,” says Stephen DeSimone, chairman and CEO of DeSimone Consulting Engineering. “At the end of the day, this is still a relationship business, and, as a consultant, I think it's difficult to answer to anyone other than our client.”



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DESIMONE CONSULTING ENGINEERING

ENGINEERING'S EVOLVING FUTURE

No matter which direction engineering firms take, it's clear that the trend toward consolidation shows no signs of slowing and the nature of the business will continue to evolve.

"The competitive landscape has changed for engineers, likely forever," Belitz says.

"Because now your competitors aren't the mom-and-pops or even the big firm down the road—your competitors are increasingly a larger, likely national firm that has professional money managers behind it that are thinking about strategically growing the business every day."

Beth Braverman is a business writer based in New York. She has worked for Money magazine and The Fiscal Times and has written for Newsweek, CNN Business, and CNBC.