PERSPECTIVE

Positioning for the future

Perspective on the built environment

Macquarie Business Banking

MACQUARIE BANK

Foreword

Shaping the built environment for prosperity and growth

The built environment is critical to Australia's prosperity, and one of the essential infrastructures that underpin the broader economy. Yet it is acutely vulnerable to structural and cyclical factors, including government policy, inflation, supply issues and rising input costs, labour challenges, and economic impacts.

Over the past decade, the industry has benefited from tailwinds of economic growth and policy, with advantageous investment in roads, bridges, mining, and education and healthcare infrastructure, as well as residential construction. Now, with the economy softening and government projects increasingly subject to cancellation or delay, questions arise regarding what next.

The built environment is at an inflection point, with business owners needing to consider their ambition, strategy, business model and plan.

It's imperative to plan your trajectory early and determine your path carefully. Understanding the factors driving your industry and sector, alongside the fundamental drivers of business value, will help you develop a plan to optimise your business and capitalise on opportunities. Be ready to recognise and harness the catalysts of growth.

In this report, we explore the current economic context that business owners must operate within, and how this impacts the businesses of engineers, architects, surveyors, planners, certifiers, project managers and consultants. In a shifting landscape for business owners, navigating the challenges that are both within and outside of your control, and positioning your business to meet opportunities, is core to growth. We will also cover how to fund growth, with options for structuring your capital.

Our point of view is based on economic research, industry data, aggregated data on file, and a comprehensive survey of businesses across the built environment sector.

There is an abundance of opportunity. How you can position yourself and capitalise on this is key.

I've greatly enjoyed working with business owners over my time specialising in structuring the growth of built environment businesses. If you have any questions, or would like to discuss your plans, our team are free to speak with you.

Danny Chung
National Head of the Built Environment
Macquarie Business Banking

Contents

Economic context

The built environment is particularly exposed to the ebbs and flows of the economy and government policy.

Subject to an array of factors, the political and economic environment has created significant demand for work, yet budget and labour shortages, along with cost increases and supply chain issues, have reduced capacity to address that demand. Additionally, businesses have lower threshold to take on more work, with project cancellations affecting revenue forecasts. Inflation has been persistent, with downstream impacts across all areas of doing business.

Within the built environment, easing inflation will increase the certainty of cost inputs, yet costs of capital and labour remain high, which could lead to more speculative projects being put on hold. Tailwinds from pandemic-era government stimuli are ending, with cancellation of significant government projects further diminishing the pipeline.

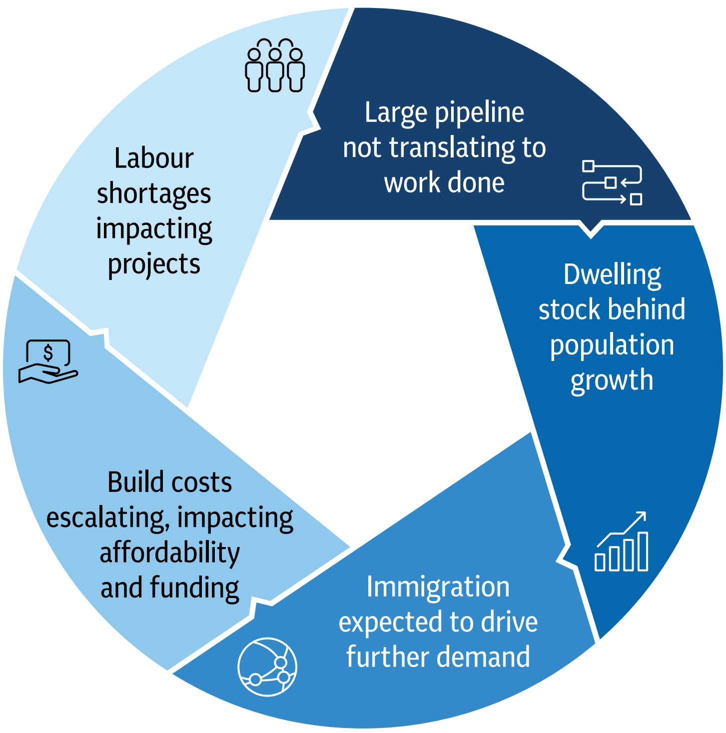
At a sector level, **residential** building approvals are lower than demand, with no meaningful uptick forecast in the near term. **Industrial** approvals remain strong, helping to address demand. Within a retail context, a return to bricks and mortar shopping, as opposed to online, has buoyed retail development. There is a trend towards **repurposing office buildings** for alternative uses.

Impact on the built environment

In the residential sector, a vicious cycle is in play, with demand regularly outpacing business capacity on all fronts.

- Population growth is outpacing the growth of residential dwelling stock, with immigration further driving demand
- The pipeline of work is significantly outpacing the volume of work completed
- A continuing labour shortage is increasing competition for skilled staff, where demand also exceeds supply: in 2023, Infrastructure Australia estimated a shortfall of 229,000 infrastructure workers.[1] This is also causing a rise in labour costs.
- Affordability amidst rising build costs is impacting projects, causing delays or cancellations as consumers are challenged to adequately fund work.

A vicious cycle



1. Infrastructure Australia, Market Capacity Report 2023, 12 December 2023.

Housing pressure is prompting government policy action, however in the non-residential sectors, the problem is opposite. Over the past decade, built environment businesses have experienced significant tailwinds from government construction projects, buffering their pipeline and bottom line. Now, as those projects are completed, delayed or cancelled, the pipeline of work for many businesses is dwindling.

Across the industry, costs are escalating, particularly materials and labour, making it challenging to correctly price jobs, squeezing margins and negatively impacting confidence across the market.

The cost of doing business in construction has risen since pre-pandemic by an estimated 40% or more.[2] The market has adopted the higher costs, with the cost of labour baked into consumer expectation.

Businesses who do not have robust finances and processes in place may experience weakening margins. We can see this in action in an increasing number of construction firm insolvencies, as a growing number of larger builders experience negative cash flows.

A positive takeout

The peak in wage growth is likely to be near, with hours worked beginning to fall from a high level.

With this in mind, what can your business do to create a sustainable path through a recovering economy, taking advantage of the opportunities it presents, rather than bearing its pitfalls?

2. Macquarie analysis; estimate.

Our perspective

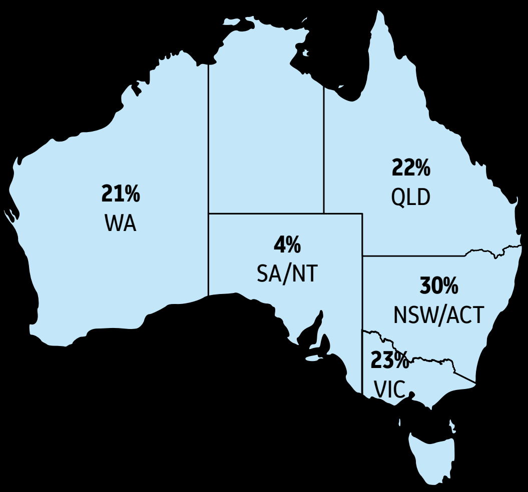
Our point of view is based on internal analysis and economic research, augmented by a comprehensive benchmarking study in late 2023, of **411** businesses within the built environment. The cohort encompasses architects, engineers, surveyors, planners, certifiers, contractors, project managers and environmental consultants.

Respondents in the 2024 Macquarie Business Banking Built Environment benchmarking study are representative of the industry in terms of dynamics, revenue and demographics.

We sought responses relating to:

- **Financial performance**
- **Business operations**
- **People and culture**
- **Clients**
- **Challenges and focus areas**
- **Sentiment and confidence**
- **Plans for the future**

A focused study of the built environment



Shifting business dynamics

Recently, the turbulence of global and local economic climates has caused shocks felt within the built environment industry. Amid this changing landscape, the landscape for business owners has also shifted, along with what is required for resilient, sustainable operations. It is unsurprising that 34% of respondents[3] were concerned about deteriorating economic conditions. How these business owners are focused on addressing concerns is paramount.

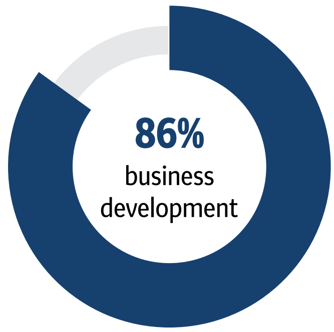
What are business owners in the built environment focusing on?

86% of respondents are focused on business development.[4] This has over twice the focus of attracting and retaining people at 42%, and streamlining business operations at 40%.

Why does business development occupy such significant focus and attention?

Business owners are focused on filling the pipeline of work to ensure productivity remains consistent despite project delays. A robust pipeline mitigates the risk of inadequately utilised staff in the event of delays, and given the substantial cost of skilled people, a focus on the future is imperative for staff satisfaction, and business continuity overall.

#1 focus area...



A healthy forward book of work:

- shapes a business' future, providing opportunities to flex if projects are delayed, e.g. redeployment of people in effective, profitable ways
- maintains stability
- appeals to potential partners, staff, investors or buyers.

Core challenges for business owners in the built environment[5] include:

Top areas of challenge for business:

A deteriorating economic environment is an additional concern, but at 34%, is less than half that of fee and margin pressure, and job and project delays.

Other challenges include attraction and retention of staff (30%) and utilisation rates (22%).

One in four respondents report escalating debtor days, which adds to cashflow challenges.

3. Macquarie Business Banking built environment benchmarking study, 2023.
4. Macquarie Business Banking built environment benchmarking study, 2023
5. All statistics regarding challenges from Macquarie Business Banking built environment benchmarking study, 2023.

The relationship between key focuses and challenges is critical. There is an intrinsic link between the focus of business development, and challenges of margin pressure and project delays or cancellation; business owners must navigate a softening economy in a high inflationary environment, with increasing interruptions or cessations to their pipeline. Developing their business' growth and scale, and thus having the cash flow, staffing, and pipeline to manage an unreliable book of work, is a clear option for many in order to weather the current economic cycles.

The business challenge

Cost escalation and margin pressures

High interest rates and input cost inflation are compressing margins, especially if projects are delayed in a high inflation environment. Cashflow and margin pressures have led to rising debtor days for one in four businesses.[6]

Project cancellations and delays

Private and public projects are being postponed and building approvals have declined. The Australian Government infrastructure review pushed through a streamlined road and rail project charter in November 2023.[7]

Staff attraction and retention

Finding and keeping specialised staff is a challenge amid an estimated 229,000-person shortage of infrastructure workers.[8] Wage inflation is compounding the problem.

Staff utilisation

Pipeline disruption makes it difficult to keep staff fully engaged and utilised.

Business owners must review their strategy. Capacity must shift to accommodate an excess of projects to fully utilise staff and provide a buffer for delays.

With many projects tendered on fixed price contracts, increasing material costs and labour market dynamics, including staff salaries occupying nearly 60% of revenue,[9] can have significant impacts on business profits. Costs may escalate while income remains stagnant in the time it takes for projects to commence.

It is imperative to create a generous buffer of ready projects within a business' book of work. Not only does this help ensure continuous cash flow and business prosperity, but it will keep staff engaged and productive, rather than on standby.

6. Macquarie Business Banking built environment benchmarking study, 2023.
7. Australian Financial Review, Full list of 50 axed road and rail projects, 16 November 2023.
8. Infrastructure Australia, Infrastructure Market Capacity 2023 Report, December 2023.
9. Macquarie Business Banking built environment benchmarking study, 2023.

People

People are a business' most significant asset, and attracting and retaining talented staff is a key issue for almost all Australian businesses. Businesses in the built environment are feeling the effects of high supply and labour costs, labour shortages, and project cancellations and delays. This can make managing the cost and efficiency of professional teams increasingly difficult, and makes effective people strategies all the more important.

Projects can't proceed and businesses can't bring in revenue without deploying highly skilled professionals. When projects are delayed or cancelled, there are three choices a business can make:

Wait for the project to start, with continuation of resourcing, but without project cash flow to support wage costs.

Reduce workforce to ease cost pressures. When the job commences, the business must compete with labour shortage and inflated wage costs to resource projects.

Redeploy staff to other projects in the pipeline.

Depending on the project, any one option could be appropriate for the business and staff involved. It's critical that your business is able to get the balance right, with levers in place to manage project cancellations and delays nimbly and flexibly:

Retention strategies beyond remuneration for key talented staff.

Maintaining a broad, diversified pipeline to allow room for staff redeployment.

A strong employment value proposition, so your business stands out when navigating the labour market.

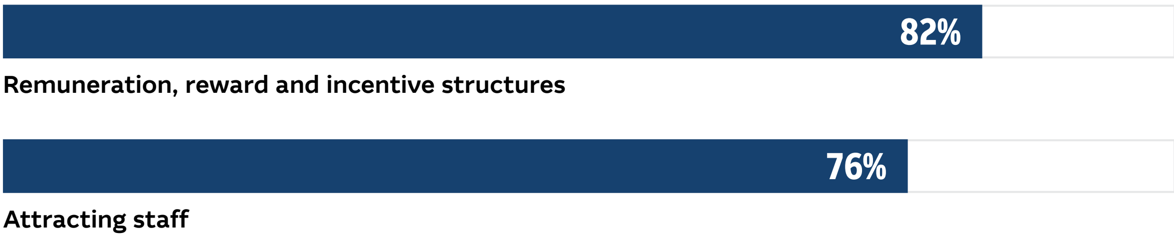
These strategies are key to managing people costs and efficiencies.

The people challenge

People costs consume almost 60% of revenue in the built environment,[10] a significantly higher portion of expenses than other professional fee-for-service industries.[11]

Navigating this high-cost environment is proving to be a challenge for most businesses, with 82% citing remuneration, reward and incentive structures as a major people challenge. Attracting staff was almost equally as challenging, with 76% having difficulty attracting talented people.[12]

People challenges



Steadily increasing remuneration to retain staff or attract new recruits is no longer an effective lever to pull, leaving businesses with the challenge of finding alternative ways to address labour shortages. At least half of these businesses are already going down this path, with 55% focusing on offering progression opportunities to staff,[13] a key strategy for motivating and retaining talented people beyond salaried pay.

10. Macquarie Business Banking built environment benchmarking study, 2023.
11. Macquarie Business Banking insurance, legal, accounting and financial services, real estate, and strata benchmarking studies.
12. Macquarie Business Banking built environment benchmarking study, 2023.
13. Macquarie Business Banking built environment benchmarking study, 2023.

Similar to remuneration concerns, project cancellations and delays may continue to impact profit margins if businesses are unable to implement effective ways of managing workload and redeploying under-utilised staff. Many are already feeling the effects of this: 55% of built environment businesses cited managing staff workflow and utilisation rates as another key challenge.[14] To remedy this, there is a significant need to consider strategies such as:

Automation or outsourcing of repetitive tasks

An appropriate ratio of administrative and support staff to specialists, to ensure that client-facing and technical teams are doing the most valuable work

The strategies you choose will differ, depending on the way you run your business, the size and structure of your teams, and your existing workflows and processes – but they remain key considerations for improving the productivity and output of your teams without outsized impact on wage and salary spend.

14. Macquarie Business Banking built environment benchmarking study, 2023.

The importance of employee engagement

Productive staff, and the expertise and service they provide to your clients, are fundamental to the value of your business, with engagement key to productivity. Ensuring that you can keep your staff motivated, inspired and willing to deliver value to your clients is critical, particularly in a competitive labour market.

The benefits of highly engaged staff

Higher work performance and productivity

Higher employee retention (lower turnover)

Greater discretionary (voluntary) effort

Improved client experience, loyalty and likelihood of advocacy and referral

Eight ways to drive higher engagement among employees

Remuneration is not the sole, or even the most important, reason employees join and remain with a business. Research[15] suggests that there are eight core drivers of employee engagement that are consistently more important to employees than remuneration, including:

Belief in leadership: Ensure leaders align their behaviour to the business' values and show continued interest in employee wellbeing. Leaders who earn trust and confidence from their employees will have an increased impact on the engagement of people who work for them, because employees will observe and echo their leaders' sentiments and behaviours. What leaders say, how they act and what they prioritise must create a supportive and safe workplace.

Alignment to strategy: Make clear to staff how their individual performance contributes to the business' goals and strategy

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Balance between professional and personal objectives: Consider ways your business can offer staff flexibility and autonomy, as this is increasingly a competitive advantage for attracting and keeping talent. Provide sufficient resources, including people, systems and tools to enable efficiency when staff are working flexibly.

Image: Cultivate a positive external brand that allows employees to have pride in the business and believe that it is highly regarded by the community

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Employment value proposition: Understand your business' points of difference as a workplace and use them as selling points to engage and retain talented people

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Deliberate and genuine interactions: Involve staff in the decisions that affect them. Empower staff to speak up. Being heard and responded to makes people feel valued.

Development pathways: Nurture the talent you have – systematically assess skills, identify gaps and invest in professional development to foster career growth

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Health and wellbeing: Offer resources to support the physical and mental wellbeing of your staff, and tools to maintain a healthy work-life balance.

15. Willis Towers Watson, Global trends in employee attraction, retention, and engagement, 2014.

Succession as a retention strategy

Succession planning is regularly used throughout other professional services industries as a tool for:

Engagement **Performance** **Motivation** **Retention**

While generally used as an exit strategy for ageing owners, succession planning can also be the ultimate way to foster the engagement and motivation of talented staff. Through succession planning, owners can identify those talented staff members that represent the values of their business, and bring them into the business' strategy and future with a strong incentive to remain and continue delivering value.

Where staff hold equity, their performance is often higher.

With their interest aligned to business goals, they're incentivised to stay, and grow their investment.

Over time, they are also increasingly included in planning the future of the business. Junior staff are looking for more than equity; they seek a greater sense of purpose in their work.

With succession planning, your employee's job is no longer just a job, but an investment in their future success – and for you, with young talent lined up to carry the work forward, an investment in the future success and value of your business. Locking people into the business, and providing adequate motivation to perform, safeguards your business stability and value, and provides staff with greater motivation and purpose in their work.

Your business' future leadership

A significant generational transfer of business knowledge and wealth is underway

58% of business owners in the built environment are over 50 years of age.[16]

25% are over 60.[17]

Aside from employee engagement, it is still important to consider succession as a way to set your business up for your eventual departure. Your business and your role in it will evolve over time. Given the investment you've made in building it, it's important to plan for the realisation of that value – to receive an appropriate financial reward for your time, expertise, and capital.

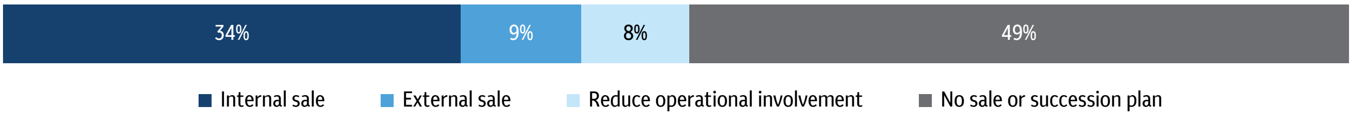
What will happen to your business when you retire?

How much value can you extract from your business if you choose to sell?

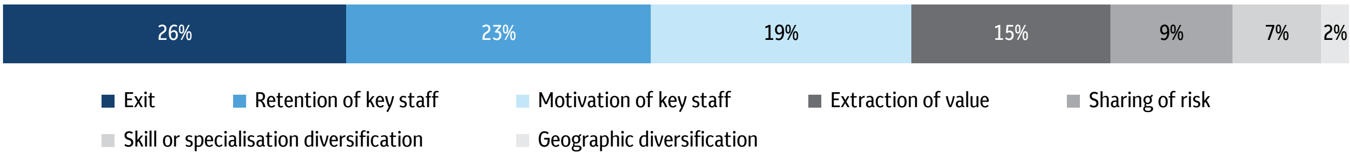
Who could potentially take over leadership from you, if you choose to pass it on to someone internally? How would this be structured?

16. Macquarie Business Banking built environment pulse check, 2023.
17. Ibid.

Succession planning in the built environment – who has a plan?



Primary motivators for succession planning in the built environment



Beyond succession planning for business leadership and ownership, another consideration is whether to scale, sell, or merge with another business. For the smaller entity, what would make the business more attractive to a larger business? In many instances, it is the skill, tenure and contribution of people that differentiates from industry peers. Those that are locked into your business through equity only further set your business apart.

Understanding how to retain and motivate talented people becomes core to business value, and future value. In an environment where the labour market is under pressure, and in an active merger and acquisition landscape, maintaining focus on people can stabilise your business, and ensure its longevity.

Diversifying the book of work across sub-sector and geography mitigates downturn risk, but the capacity to flex into this type of opportunity, effectively engaging and utilising their people, represents a fundamental question for business owners: **scale or specialisation**?

Scale or specialise?

When planning for the future, it's impossible to predict where work will be most abundant, especially when considering the interplay of economic, policy, staffing, environmental and social factors. Knowing how to shape your business to meet opportunities in profitable ways is an enduring challenge.

Markets are increasingly challenged, driven by asset class, owner, and geography. Within this context, business owners are considering options to reduce volatility and the impact of uncontrollable elements.

At some point along the growth trajectory of a business, questions arise regarding whether to be niche, focused and specialised, or scale operations to capture adjacent or new opportunities. There are strong cases for both business models.

Why would you consider expansion or scale?

- **Expansion across new disciplines**
- **Liquidity event**
- **Attraction and retention of talented people**
- **Diversification of business model**
- **Implementation of new systems and processes**

In high-performing businesses, innovation is essential for sustainable, profitable growth. Within the parameters of high performance, there is a drive for scale, either through organic growth, merger, or acquisition. Scaling operations across discipline and geographic areas allows for capturing new business, expanding into new disciplines, attracting and retaining great people through offering diversity of work and jobs, and making a business more attractive at sale or merge. For many owners of high performing businesses, it is core to their strategy.

Our point of view is that scale enables your business to:

Grow in pipeline capacity
Spread risk across more work, to cushion the impact of project delays

Diversify book of work by sub-sector, size or geography
Credibly take on more and larger projects in areas with the highest demand

Build business development and marketing capability
Scale justifies specialist business development, expansion of administrative roles, and technology investment

Attract talent
Larger businesses may offer stronger employer branding and more career opportunities, attracting larger talent pools with more experience and skill

Reduce key person risk
Scale enables principals to spend less time on tools and plan for growth and succession

Create a liquidity event
Capture the opportunity to extract value from your business

The small vs scale paradox

Business owners must make choices.

Specialise

Allows a business to be more autonomous and nimble, but may leave it more vulnerable to external factors if it is limited in capital and resource.

or

Scale

Brings advantages, but also raises costs and may require a business to balance more risk.

Small business owners may benefit from specialisation in highly profitable niches, but may be disadvantaged, given the nature of the small business model provides limited capacity to capture new opportunities and fill this niche pipeline.

So how do you determine the right scale for your business?

There are advantages and limitations for both, and choices for how you can enable scale in your business.

Sources	Small business	Large business
Advantages	• Highly specialised • Autonomy of owners • Business agility; unencumbered by systems • Niche market or client base • Business development driven largely by word of mouth and relationship	• Could be diversified, or highly specialised • Ability to pivot and redeploy staff if projects are delayed or macro factors shift • Attraction of staff may be easier due to a stronger market presence • Retention of staff may be easier, due to ability to pivot into new areas, and exposure to diverse projects • Scale bolsters business valuation, creating opportunities for owners through succession, equity, or sale
Limitations	• Limited market presence and tools • May only have capacity for a small number of projects • Key person risk • Key client risk • Vulnerable to project delays or factors outside of their control • Pivot into emerging areas may be difficult, given resourcing or skill gaps	• Requires volume of business to survive • Significant overhead costs • Higher exposure to risk • Need for more complex business model • Lower autonomy

When businesses grow, they may carry additional risk. As a result, growth strategies need to be carefully planned and managed, with adequate and appropriate finance to minimise risk in the face of unforeseen market changes.

What are we seeing?

Sectors within the built environment are in a consolidation phase, with abundant merger and acquisition activity providing opportunities for business owners and their people.

Businesses are getting bigger

There is a strong case in the industry for either a highly scaled or highly specialised business model, to avoid being ‘caught in the middle’, competing with both ends of the market. Businesses with between 10 and 50 staff find themselves competing for projects against the small and the large businesses, without the agility and lower cost structures of smaller businesses, but lacking the resources, reach, and recognition of larger businesses. This is a key motivator for owners to scale.

The generational shift is underway

Owners are looking within their business for the next phase of ownership, with an end goal of realising the value of the business asset that they’ve created.

Locking talented staff into an equity holding position not only helps with retention issues, but can also increase options for sale and increase asset value with higher multiples offered by buyers.

The trajectory of change

For Australian built environment business owners to fully embrace scale and transformation, there must be a path to profitability – a roadmap for culture, process and technology changes.

What you can't control

Economy
Project cancellations
Labour dynamics
Government policy

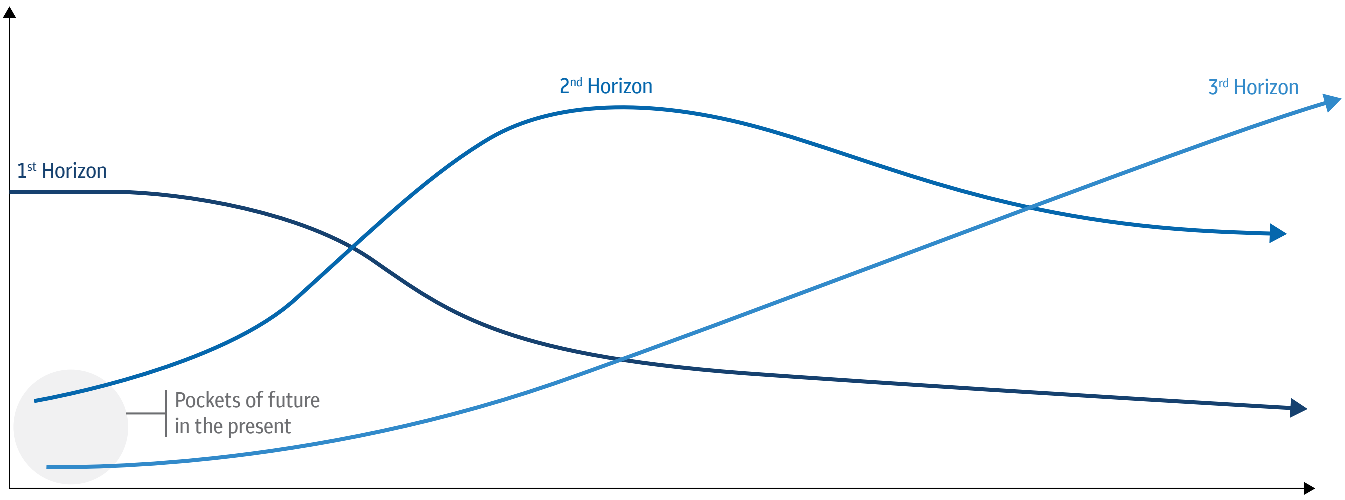
What you can control

Business strategy
Culture and purpose
Succession
Size and scale
Client focus
Sectors of operation

The need to innovate

Innovation is essential for growth. This is because maintenance of current ways of doing business becomes less sustainable over time, due to competition shifting consumer expectations, and the increased cadence of change in a broad sense. What was impressive for consumers ten years ago becomes a baseline expectation over time; it is critical to improve upon value and client proposition as the business climate evolves.

Three horizons in the present[18]



Three horizons in the present (Bill Sharpe) shows how businesses and individuals may haul "pockets of the future in the present" through experiments and innovation at the confluence of BAU and transformation

18. Three Horizons: The Patterning of Hope: Bill Sharpe, 2013.

The 'Three horizons in the present' model illustrates how business must innovate. It has three 'horizons' or assumptions:

01	**First horizon** Business as usual delivery of once-profitable services that decline in value and popularity over time, due to innovation and competitive forces.
02	**Second horizon** Rapid improvement and transformation, unshackled from practical considerations.
03	**Third horizon** Incremental improvement realised as a result of the tension between the first two horizons.

Many business owners maintain their focus on delivery within the first horizon; delivering work in ways that satisfy client needs and maintaining a steady volume of new work. However, over time, this becomes less profitable, given that competitors may innovate around this offering, providing work in new ways, at greater speed, quality or lower cost.

Within the context of innovation and scale, a business that does not experiment risks becoming less relevant or competitive; others may encroach into what was once a differentiating service or offering, normalising either what you do or how you provide it. To succeed beyond this, it's crucial to understand what you do, how it's perceived by clients, and the value that it delivers, then innovate around it. When done successfully, this may provide opportunities for your business to extend its offering and further differentiate.

Options for scale

Choosing an appropriate growth strategy can help you create a more resilient business, while creating enduring value for yourself, staff, and clients.

There are a number of pivot points to scale, with fundamental questions regarding how you will enable growth:

Organic growth

- How will you drive business development and incremental growth?
- Will you be able to capture opportunities as they present?
- Will the systems, processes, people and strategy you have in place support growth?

Acquisition

- What are your merger and acquisition opportunities?
- Will the business you merge with or acquire be a strong fit for your business?

Succession

- Who are your high potential team members?
- Are these people aligned to your business' strategy?

Funding

- How will you fund your growth plans?

If considering scaling your business, it's imperative to assess and agree how you plan to grow.

Planning your business' evolution

By planning and putting the appropriate structures in place early, you can accelerate growth, and realise your ambition sooner. The choices you make will determine how you can:

Grow or scale your business

Borrow money from lenders and borrow on more advantageous terms

Share equity, or create profit share models, which may attract investors or directors

Attract and retain talented staff

Cope with changes in the wider business and economic landscape

Reduce your time in your business without having to dismantle the business structure or effect some other radical change

We find that there is no shortage of opportunity to capture. The question is, how do you prioritise the choices and structure your business best, to realise maximum value?

Core drivers of business value

Understanding what influences your business' value is key to growth foundations.

Focusing on the drivers of value to understand and optimise the value of your business improves the financial outcome of any option that you choose, such as:

- **Positioning your business as an attractive merger partner**
- **Attracting a higher value if you choose to sell all or part of the equity in your business**
- **Borrowing on more advantageous terms if you invest or scale up**
- **Attracting a higher valuation when you borrow money for growth**

Drivers of value

Diversity of earnings

How many directors or specialists are involved in your business? How varied is your book of work, and the services you deliver?

Barriers to entry

Is your business defensible? How difficult would it be for a competitor to replicate what you do?

Client profile

Who are your clients? How strong is your relationship with them? Do they refer business to you? What is the strength of this referral or business development? How is new business generated?

Quality of earnings

Is your revenue reliable and consistent? How does your business manage project planning and revenue?

Quality of staff

How long have your people been with your business? Are you nurturing a new generation of leaders?

Macro factors

What is the broader business outlook? Are there factors driving activity in your sub-sector focus or geographical area? For example, are you benefitting from population growth, demographic factors or local policy?

Financing growth

If you have made the decision to scale your business, there are a number of different ways to enable its growth.

	Organic growth	Funded growth
Sources	Grow your business via investing existing capital and resources.	Grow your business via: • Debt finance – Bank lender – Non-bank lender • Equity finance – Internal equity – External equity
Advantages	• Lower risk over a longer horizon • Leverages existing talent and resources	• May help you achieve business goals and personal aspirations sooner • As your business grows in scale and sophistication, your finance options grow, enabling greater access to capital, on more favourable terms
Limitations	• Your business may not be ready to capitalise on opportunities as they present • Market or competitive environment may evolve more rapidly than your business' ability to capitalise on your strategy	• Debt is carried in the business or by owners • Some control may be lost, depending upon which type of finance you choose

Choosing the right finance mix

The mix of finance you select will affect not only your cost of capital, but also the degree of risk you accept, the amount of control you surrender, and the future value of your business when the deal is complete. As a result, there is no one-size-fits-all solution.

The fundamental choice is between equity and debt.

Ultimately, what it really comes down to is cost of capital versus risk, and that equation will be different for every business.

You might be hesitant to consider funding because you're cautious about your work pipeline. Yet scale can help you fill your pipeline and cushion the impact of project volatility, enabling you to be large enough to ride out fluctuations in the economy.

We can help you determine the optimal funding mix for your business and your objectives. We look at your business in the same way you do, as a profit-generating enterprise, not just a list of assets. So, we can offer you flexibility and a wide range of funding options based on your true enterprise value, rather than your balance sheet.

Finance options

Debt finance

Sources	**Bank lender**	**Non-bank lender**
Advantages	• Potentially less expensive than non-bank lenders • Broad suite of financial products to choose from • You retain ownership and decision-making control of your business • A broader relationship, across personal banking, wealth management, business banking, investments, and perspectives from experts beyond banking	• Lender may have higher risk tolerance • May be faster loan application turnarounds
Limitations	• Adds debt to the balance sheet of your business. Implications will be a mortgage or personal property security register over company assets, director guarantees and interest costs, which may place stress on cashflow	• May be more expensive • Adds debt to the balance sheet • Risk threshold may put business owners under increased pressure

Equity finance

Sources	**Internal**	**External**
Advantages	• Retention of key staff may be built into model • Alignment of incentives	• No debt on the balance sheet • Potential access to outside expertise
Limitations	• Typically sell equity at a lower valuation • You share control and decisions	• Dilutive to shareholders (benefits will be shared) • Potential loss of control

Debt finance

Borrowing to grow your business is an opportunity to make the most of the assets you've accumulated, including the business itself and its ability to generate earnings. Broadly, debt finance can be:

Secured

Finance underpinned by assets such as property, either residential or commercial, offered as security to the business loan, together with personal guarantees. Most often used by small to medium businesses, secured debt may be both less expensive and more limited than unsecured alternatives.

Limitations include choices that can be made with the assets secured against the loan, which may be unsatisfactory to other parties, particularly if the asset is the family home.

Unsecured or non-recourse

Lending is against the historical performance and profits of a business, which implies the ability of the business to operate profitably in the future. Assets such as the family home are not required to grow or scale the business. For built environment businesses, borrowing this way can simplify the lending process if sufficiently planned and considered. This may be particularly attractive to growing businesses with higher capital needs, as they may have fewer assets to offer as security.

Bank debt

Borrowing from a bank is the most frequently used financing model. Banks typically offer a wider range of options, each designed for a specific purpose, and may be able to lend at lower rates than non-bank lenders.

A banking partner can support you as part of a holistic relationship that addresses both your business and personal needs. This can include structured lending across both personal and business entities to help deliver favourable cash flow and tax outcomes for you and your business.

Non-bank debt

Several non-bank lenders are active in the built environment. Non-bank lenders may offer greater flexibility and higher risk tolerance than a bank. However, that flexibility may come at the cost of higher interest rates and a narrower relationship, without the benefits of a broader product range and advice.

Equity finance

Alternatively, you can sell some of the equity in your business, either internally, to one or more colleagues, or externally to a new partner or investor. This may be an attractive option if you wish to leverage the business knowledge of more experienced investors. The obvious benefit of this model is that there is no loan to be repaid and no liability on the balance sheet. However, it also means you share future profits and, potentially, control of the business, perhaps with an investor whose goals and timelines are different from your own.

Finance as a growth catalyst

There are three main ways we see built environment businesses using finance as a catalyst for growth:

Mergers

Joining with a business with complementary strengths to increase scale. Finance can smooth the transition phase and fund investment into the systems, tools and capabilities needed to operate at a larger scale.

Acquisitions

Using finance to purchase existing businesses and incorporate them into your business. The aim is to add scale, bring in new skills, sector expertise, geographical coverage or client relationships to add value to the existing business.

Establish in a geography with access to a new market

Expand by opening an office in a geography with growing opportunities and the need for on-the-ground services. This could mean sending professionals from your office to establish an office in the new location or partnering with a local business to harness local knowledge. Finance can offset what is sometimes called trade-up risk – leasing, staffing and operating costs until the new site generates enough revenue to support itself and makes a positive contribution to the larger whole.

Replenish capital and reward investors

Using finance to capitalise the business and enable current owners to 'take money off the table', by returning capital to investors or buying out significant shareholders. Bear in mind that it's possible to achieve more than one growth objective at once.

Appealing to lenders and investors

Unless you borrow against security, lenders and investors typically approach your business in a similar way, by valuing it as an enterprise, based on your current earnings and an appropriate multiple of earnings. That means you can maximise your finance opportunities and make your business more attractive to lenders and potential investors by focusing on key value drivers. Some key strategies for structuring your business to attract funding and facilitate growth include:

1. Demonstrate sound financial and corporate governance

Start by ensuring your accounts and financial reports are complete, compliant and well substantiated, then make strategic decisions in line with the information they provide.

2. Focus on key performance metrics

Increase your business valuation and lending capacity by maximising these key indicators of financial importance:

- **The predictability and stability of business earnings**
- **Profit margins:** careful management of expenses
- **Revenue and profit trends:** are the business earnings and margins increasing?
- **Capital intensity:** the amount you need to invest to continue running your business compared to another business of the same type

3. Have a clearly articulated plan

Show how you'll harness the extra capital to add value. For example, if you're planning to grow by acquisition, show how you will integrate the target business into your existing business and increase its value.

4. Build a strong culture with good staffing practices

Incentivise staff to stay with the business by having a supportive workplace culture that encourages communication and productivity.

5. Create alignment

Offering equity to key staff may strengthen staff retention and enable your business to extract greater value from its significant investment in salaries.

What next?

Determine your business' ambition. Align owner and director objectives to business strategy. Document it succinctly. Communicate your plan with staff and stakeholders.

Are you seeking to scale, or be specialised? Be mindful of being 'stuck in the middle', where you compete against smaller businesses with lower cost structures, and larger businesses, with greater resources, reach, and recognition.

Work with talented people; bring them into business strategy early, and offer them a sense of higher purpose when considering equity involvement.

Focus on pipeline. It will drive your business, and the people who work in it.

Align owner and director objectives to business strategy.

Ensure that your business' culture is conducive to growth and productivity.

Reduce friction in operations. Focusing on efficiency drivers, and cost minimisation, is important in a shifting economic climate.

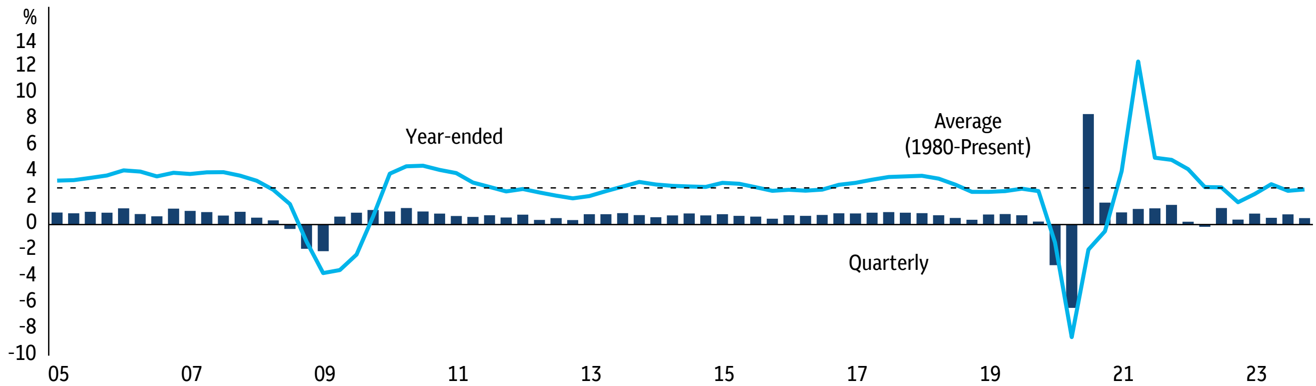
Appendix

Global

Given the volume of investment capital that flows from the United States of America (USA) into the Australian economy, the outlook for the USA has a salient influence on Australian business.[19] Our observations are:

- Easing financial conditions have significantly reduced the risk of a USA local recession. This has triggered a delay in USA interest rate reductions

Global GDP Growth* - Market exchange rate weighted



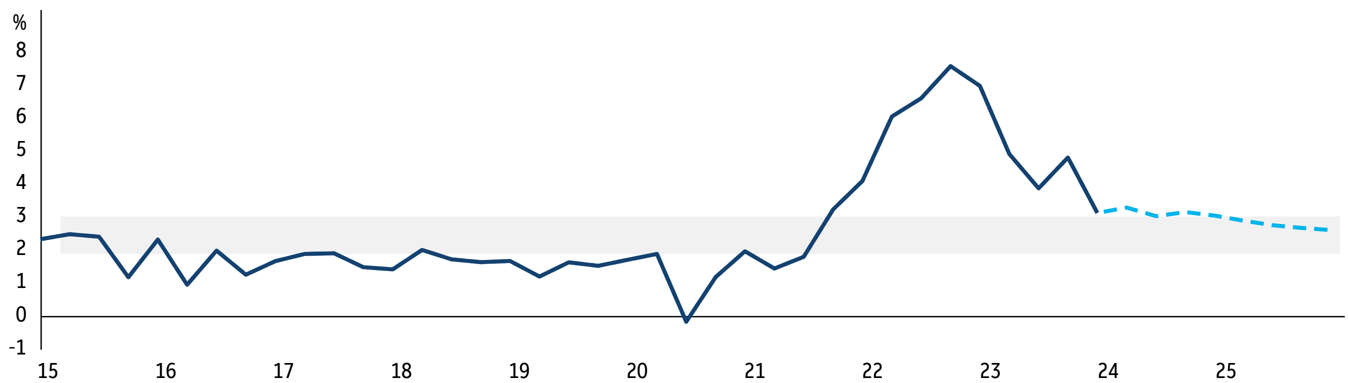
Source: Reserve Bank of Australia statistics, Macquarie Group internal estimate. *Latest observation based on actuals where available and Macquarie forecasts otherwise.

- Despite higher interest rates, global output remained resilient in 2023, with gross domestic product (GDP) growth sitting around its long-run average
- USA manufacturing levels have stabilised, with real goods consumption, which is consumer money spent on goods and services, growing from an already elevated base
- Continued labour market resilience implies that USA unemployment levels of around 3.4% are likely to persist.

Local

Inflation in Australia has been more persistent than in the USA, and remains high, with downstream impacts on all Australians.

Australia - Quarterly Trimmed Mean Inflation Annualised



Source: ABS, Bloomberg, RBA, Macrobond, Macquarie. * Dashed line represents RBA February 2024 SoMP forecasts

19. AFR, It's America that's investing in our future, 20 August 2020.

Industry

- High interest rates will continue to cause pain for the built environment industry
- Easing inflation will increase the certainty of cost inputs, yet costs of capital and labour remain high, which could lead to more speculative projects being put on hold.
- Tailwinds from pandemic-era government stimuli are ending, with cancellation of significant government projects further diminishing the pipeline.

Outlook by sector

Residential

- Housing prices continue to rise despite stretched affordability levels
- Residential building approvals remain low
- Macquarie analysts don't foresee a meaningful uptick in residential property projects until late 2024

Industrial

- Industrial approvals remain strong, helping to address demand
- Vacancy levels have been rising since 2023 and are expected to continue to do so over the medium-term

Retail

- A return to bricks and mortar shopping, as opposed to online, since the pandemic has buoyed retail development
- The supply of new retail property is forecast to decline through to 2025

Office

- Office vacancy rates in Sydney and Melbourne have reached multi-decade highs and are forecast to further increase
- Demand is expected to recover by 2025-2026
- There is a possibility of office buildings being repurposed for alternate uses

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How Macquarie can help your business evolve

We work with business owners to help them navigate a changing market, build resilience into their business model, and position their business for the future. Talk to us to find out how we can help you evolve your business by:

- Adding scale through a strategic merger or acquisition
- Adding diversity and resilience by expanding into a new market or geography
- Extracting value while growing your business by seeking outside investors
- Locking in skilled staff and ensuring a smooth succession by selling equity to internal leaders

To find out more:

Contact your Macquarie Relationship Manager, call 1800 442 370 or visit macquarie.com.au/built