

SURVIVING AND THRIVING IN THE MIDDLE: 4 STRATEGIES TO BEAT THE MID-TIER SQUEEZE

A COMMERCIAL BANKING PERSPECTIVE

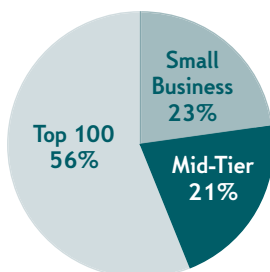


THE SQUEEZE: NEW NORMAL

Mid-tier government contractors are too big to be small – and are thus ineligible for mandated government contract quotas – and too small to be big, missing the benefits of scale that drives both business development reach and operational cost efficiencies.

Industry giants can often leverage reputation, economies of scale and resources to keep themselves competitive through the uneven business cycles of the government services industry. Plus, as government contracting opportunities constrict, these titans come down market to fill their capacity, bidding on smaller contracts and driving price downward. On the other end of the size spectrum, smaller firms are often quicker to innovate in specific areas than more established firms – in addition to benefiting from federal preferential contracting.

Allocation of Federal Government Contracting Dollars



Source: Federal Procurement Data, Fiscal 2013

In the battle to win their share of federal government contracts, mid-tier firms are squeezed between small businesses that can benefit from federal government preference programs and large businesses that can apply their size and strength.

Federal Support for Small Businesses

Today, federal small business preference programs seek to award 23% of all U.S. government contract dollars to small contractors, most with more than \$10 million in revenue. And lawmakers are considering increasing the small business contracting target to 25%.¹

While these programs may help offset the dominance of the industry giants in the government services sector, they may not be achieving the goal of ensuring diversity in the contractor marketplace. An analysis of awards by contractor size shows that mid-tier firms win the lowest share of government contract dollar value. The volume of mid-tier wins appears below both current capacity and growth potential of the middle market government contractor segment. Some argue that the well-intentioned small business preference programs are actually serving to artificially disadvantage the middle.

Advocacy Response for Mid-Tier Falls Short

Several industry groups have taken up the mid-tier contractor cause. For example, the Mid-Tier Advocacy Group is pushing for legislative action to eliminate current competitive disadvantages by establishing mid-tier “set-asides” that parallel the small business programs. The Association for Corporate Growth recently launched the bipartisan Congressional Caucus for Middle Market Growth to give the middle market a voice on Capitol Hill. Additional leveling actions under consideration for the mid-tier market include

- Revising the definition of small business to improve consistency and encompass some mid-tier providers
- Closing loopholes to preclude Fortune 500 firms from acquiring small business contracts

While the advocacy response is well intentioned and momentum is mounting, it's not enough to impact the current rules of engagement. To survive and thrive, mid-tier companies need to be smarter, more focused competitors to better manage the challenges of being too big to be small, and too small to be big. Here are four strategies to consider.

1. Never stop bringing innovative ideas.

In the current environment dominated by price competition and protests, new thinking and more effective approaches are required to break through. If you wait for the rebid or RFP, you'll be competing on price rather than value. To win, grow value through relationships with program managers to demonstrate your capabilities and point of view. This approach can help you to shape the proposal, demonstrate your delivery of a higher return on investment, and establish credibility and trust. What's more, staying in touch with program managers off-cycle helps strengthen the relationship and will give you a deeper understanding of their needs and priorities when it comes time to bid.

2. Focus on being the best at some things, rather than appearing capable of doing anything.

For a mid-tier government contractor, targeting the right pursuits and building market leadership to match is a key to success. Government agencies value depth of experience and specialization. As your firm grows, more specialties can be added, but trying to be all things to all government agencies can dilute the strength of your key capabilities.

3. Scale up to improve cost competitiveness.

Today's low interest rate environment makes it especially attractive for mid-tier companies to finance acquisitions focused on increasing market share or securing footholds in specific capabilities or government agencies. Large companies are spinning off niche business units to focus on core expertise and optimize for profitability, offering a window for strategic thinkers at mid-tier firms to snap up capabilities that deepen or broaden offerings. Strategic expansion can enable you to augment current services and fortify your competitive position.

4. Consider strategic partnerships to increase value.

Good teaming agreements can be beneficial to both parties when complementary capabilities increase the companies' combined competitive value. To maximize the benefits of partnership, be sure to first prepare your company for financial and operational fitness before seeking a value-added match.

In gaining access to additional capabilities, increasing revenues and capturing greater market share, such arrangements can take the form of partnership with a larger startup or small business. Alternatively, merging with the right partner or engaging in an all out sale could also be options if corporate directions, personal priorities or succession planning vectors align.

In the case of a sale, it's important to court the right buyers, capture maximum valuation and make post-deal integration a discussion early in the planning stage. If mismanaged, it can lead to employee disengagement, key talent attrition and business development atrophy – eroding the value of the transaction for buyer and seller alike. With the appropriate planning, the right deal can accelerate growth of the merged entity and generate greater return for all parties.

MID-TIER SUCCESS BREEDS BEST-IN-CLASS

Much of what makes mid-tier companies so efficient and effective is the precariousness of their position, forcing a combination of strategic forethought, smart focus, real time decisioning and excellence in execution. The middle is the proving ground for best practice, truly competitive government services firms. It is where organically grown firms mature into sustainable success stories... where high-performing top tier carve-outs go to gain greater efficiency...and where successful small providers evolve into the next generation of government services providers.

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¹ "Small-business quotas could become even tougher to meet," FCW: The Business of Federal Technology, February 6, 2013