Deltek Clarity

Government Contracting Industry Study

12th Annual Comprehensive Report

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Introduction

The 2020 Deltek Clarity Government Contracting Industry Study revealed that the optimism expressed for industry growth prior to the COVID-19 pandemic continues with companies' expectations for 2021.

2020 was a year of triage, disruption and reprioritization. Companies focused on business continuity and customer fulfillment while managing the challenges of a remote and distributed workforce. However, the outlook is bright with more than seventy percent (70%) of companies in this year's Study expecting that their government sales will increase in 2021. Significant growth is expected in key industries such as information technology (IT), professional services, healthcare, and potentially architecture, engineering and construction (AEC) particularly if federal infrastructure legislation being developed at this writing is passed.

The resilience of the government contracting industry was proven again in 2020, demonstrating that defense-oriented businesses are less sensitive to economic pullbacks given heavier reliance on credit markets, consumers and commercial markets relative to other businesses. Despite uncertainty regarding federal stimulus program disbursement and a change in administration, the industry held firm in the face of lower contract values and contract delays. Overall, successful performance within the industry depended on industry focus, with large-sized companies seeing less of a downturn relative to smaller businesses.

Performance is expected to fluctuate further based on the degree to which a business benefits from stimulus spending.

Key challenges for 2020 included:

- The need to prioritize the "must-have" investments, such as operations that directly support customer needs and revenue streams (e.g., project management and business development). This often occurred at the expense of support function investments characterized as "nice to have," like risk management or other tools and technologies with longer-term potential, like artificial intelligence (AI) and machine learning.
- The development of management structures and methods to successfully oversee a distributed workforce while deploying the right tools to promote virtual collaboration and sustain customer communications.
- Being smarter about financial execution by maintaining focus on the fundamentals and business continuity. Also a priority, process optimization and managing risk, given the likelihood of a near-term impact to financial results.
- Continued competition for the best and the brightest in hiring and retention as companies challenged employees to work in new ways and do more with less.

The imperative to stretch limited resources emphasizes the need to invest in and utilize the best and most up-to-date technology tools to drive efficiency. The continued reliance on "do everything" tools such as Microsoft® Excel, which are more limited and not necessarily designed to handle complicated and specialized tasks, inherently limits the information and analysis available to support decision making.

Respondents to the 12th Annual Study expressed optimism about 2021's growth potential.

About This Study

Deltek conducted an online survey of government contracting companies to explore and understand the key issues and trends that affect the industry and the outlook for 2021. The Survey was developed in close consultation with industry experts.

The findings of this Study reveal a concise picture of the challenges, opportunities and benchmarks for government contractors.

The areas explored by the Study include the effects of the COVID-19 pandemic, business development, finance and financial compliance, project and risk management, human capital management, contract management and procurement, and information technology (IT) and cybersecurity. The findings of the Survey tell the story of an industry's response to a global pandemic and its outlook for the near future, along with the challenges and opportunities that affect government contractors.

The Survey was developed in partnership with CMG Consulting, which conducted the online survey with executive decision makers at government contracting companies. The Study was fielded from January 11, 2021, through February 26, 2021.

A wide range of companies participated:

- Twelve percent (12%) of respondents are active in both federal and SLED markets (state, local, kindergarten through grade 12 and higher education). Forty-nine percent (49%) of respondents are active solely in the federal market, while 39% operate solely in SLED markets
- Forty-five percent (45%) of respondents have revenue of less than $20 million and are described in this Study as small businesses. Twenty-nine percent (29%) range between $20 million and $99.9 million in revenue and are categorized as medium-sized businesses. Large businesses fall into two combined revenue categories of $100 million to $999.9 million and more than $1 billion in revenue – 15% and 11% respectively.

The three largest industry functions represented in the Study are IT (26%), professional services (19%), and defense, weapons, aerospace or manufacturing (19%).

The respondents represent a broad geographic distribution:

- 34% are from the Washington, D.C., Maryland and Virginia area
- 26% are from the South
- 18% are from the West
- 11% are from the Northeast
- 11% are from the Midwest.

Executive Summary

Despite the challenges of the pandemic, increased federal spending softened the impact on the government contracting industry as a whole. Successful performance within the overall industry, however, varied based on strong pre-existing customer relationships and stimulus spending.

Federal spending was buoyed in 2020 by record discretionary appropriations and the government response to COVID-19. Civilian spending increased by 19%, while defense spending rose by 10%. Fifty-three percent (53%) of the overall increase was due to COVID-19. As a result, the industry held firm overall given market dynamics and disruption. However, some companies found themselves in areas deemphasized due to COVID-19, while others found themselves in fast revenue growth areas as a result of being aligned with government response efforts.

Executive focus narrowed in 2020 to business continuity and customer fulfilment, in other words, keeping operations going, meeting health and safety requirements and meeting key contract obligations. Companies put the spotlight on driving profitability and net revenue while making the most of limited business development resources. Some support functions were sidelined and headcounts were reduced, leaving remaining staff to balance top priorities.

The requirement for workers to take on more responsibilities during the pandemic emphasized the need for businesses to retain top talent and to the greatest extent possible compete successfully for capable and productive new hires. Adding to this challenge was the immediate need for a distributed workforce operating in remote locations, resulting in new management needs, such as managing a virtual workforce, and a greater focus on cybersecurity compliance.

- Diversification of products, services and markets key to increasing growth
- Normal ways of networking and building relationships with partners at industry conferences were upended, causing companies to seek market intelligence for teaming.
- Investment in more robust tools and training necessary to upgrade operational capabilities
- Migration of data to the cloud increasing significantly
- Cybersecurity compliance growing in importance, with Cybersecurity Maturity Model Certification (CMMC) requirements on the near horizon
- Positive lingering effects of remote work attractive to top talent

** Source: FPDS, Deltek*

Goverment Contractor Confidence Index

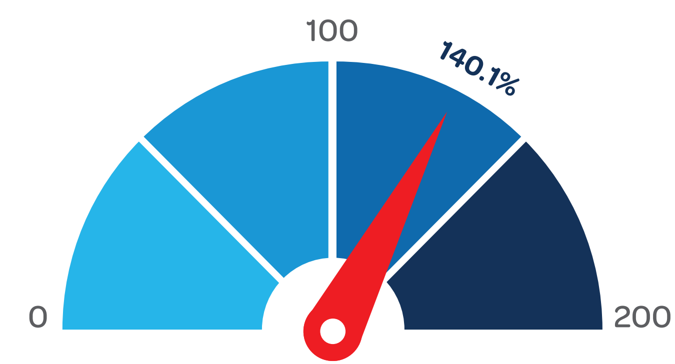
The composite Government Contractor Confidence Index (GCCI) indicates high confidence in sales for the coming year but is not as robust a sentiment as in 2019 before the pandemic.

The GCCI measures overall confidence that government contractors can grow their public sector sales over the next 12 months. It is measured on a scale of zero to 200, with zero indicating the lowest confidence level, 100 reflecting neutral confidence and 200 indicating the highest confidence.

The calculation is based on a series of questions regarding government sales in the last 12 months and respondents' impressions of the spending environment. While the index is subjective based on opinion, it is indicative of the level of risk business leaders see in the marketplace.

This year's Study shows a GCCI score of 140.1, which is a decrease of nearly three points from the 143.0 registered in 2019. The effects of the pandemic and the related economic consequences have most likely affected expectations for the coming year, which remain strong. The federal market remains stable, while the SLED environment is still uncertain with the anticipation of stimulus dollars. While 2020 was challenging, respondents are optimistic about 2021.

Government Contractor Confidence Index

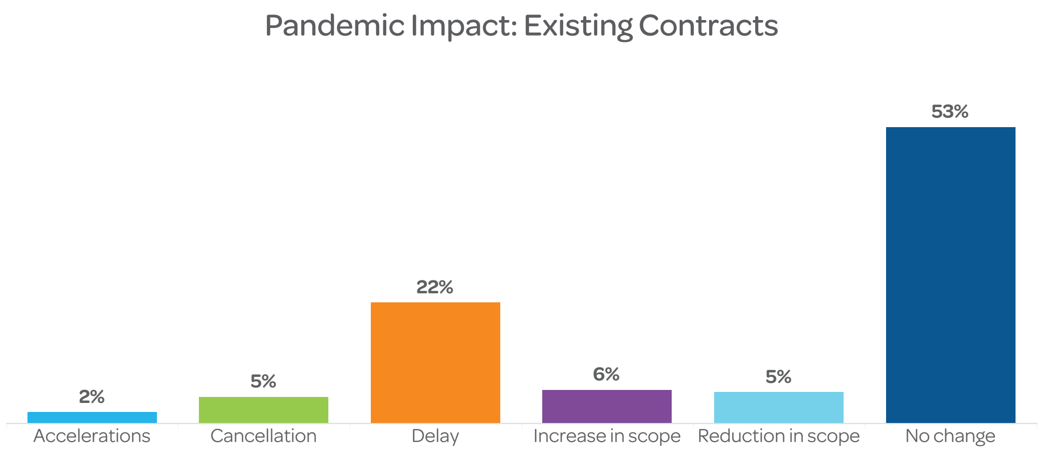


Business Impact from the Global Pandemic

As a result of the pandemic, respondents indicated increased investment in and adoption of Online Meeting platforms, Collaboration tools, and Cybersecurity technologies.

Pandemic Impact: Existing Contracts

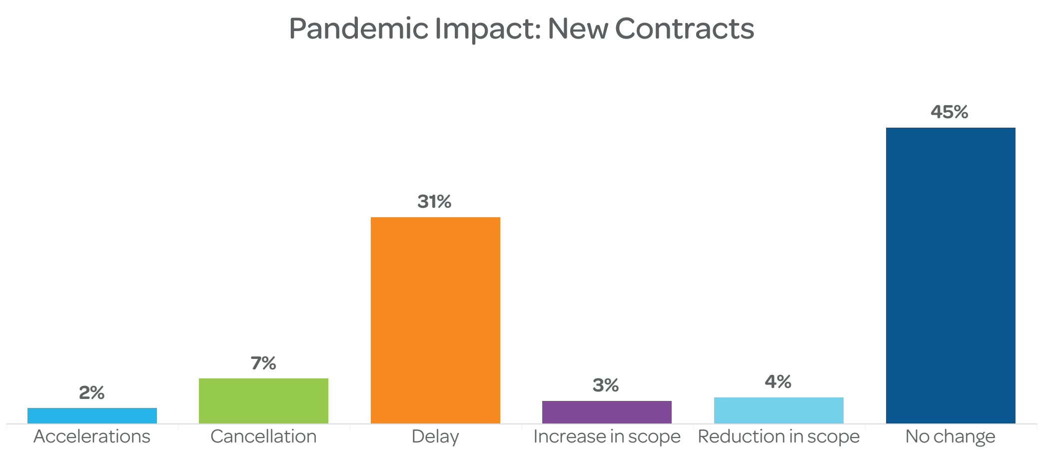
The effects of the global pandemic, while not insignificant, were somewhat less dramatic than might have been initially expected. Outside of modest contract delays – from awards to execution – government contracting businesses did not experience a significant change in new or existing contracts in 2020. Average dollar values for awarded proposals, however, dropped substantially.



Pandemic Impact: New Business Contracts

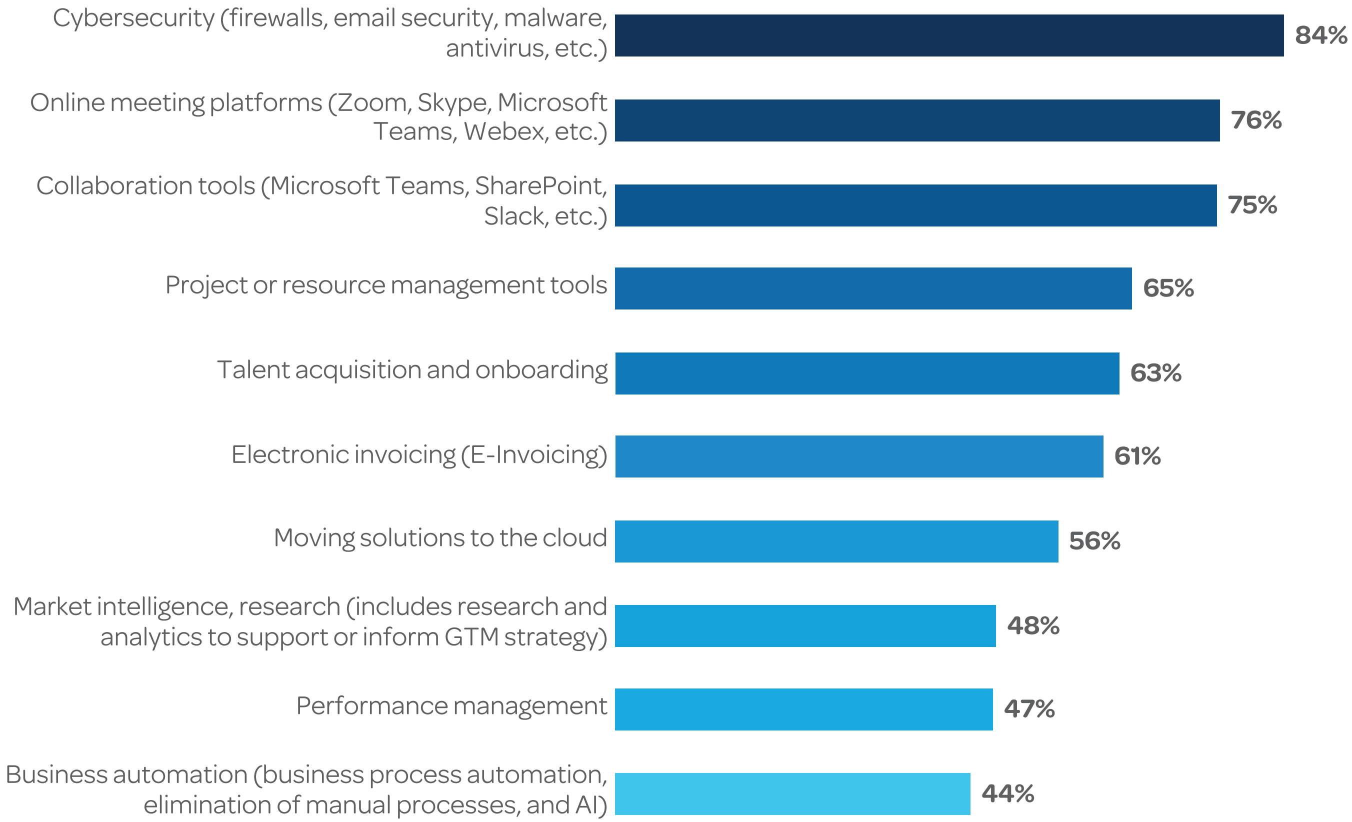
During the pandemic, companies benefitted from the multi-year nature of contracts, which helped preserve an ongoing revenue base. Through focusing on operations and adapting rapidly to support a workforce that was becoming increasingly distributed, businesses were better equipped to weather the storm. The degree of prosperity, however, was uneven with small businesses not faring as well as their medium and large-sized counterparts.

New business contracts were often delayed during the period, with nearly a third of respondents indicating a delay in 2020. That said, almost half of respondents said there had been no change, and only 7% of new contracts were cancelled. Markets that were more affected by these delays were in the federal and professional services spaces, while health care, architecture and engineering and energy/power were less so.



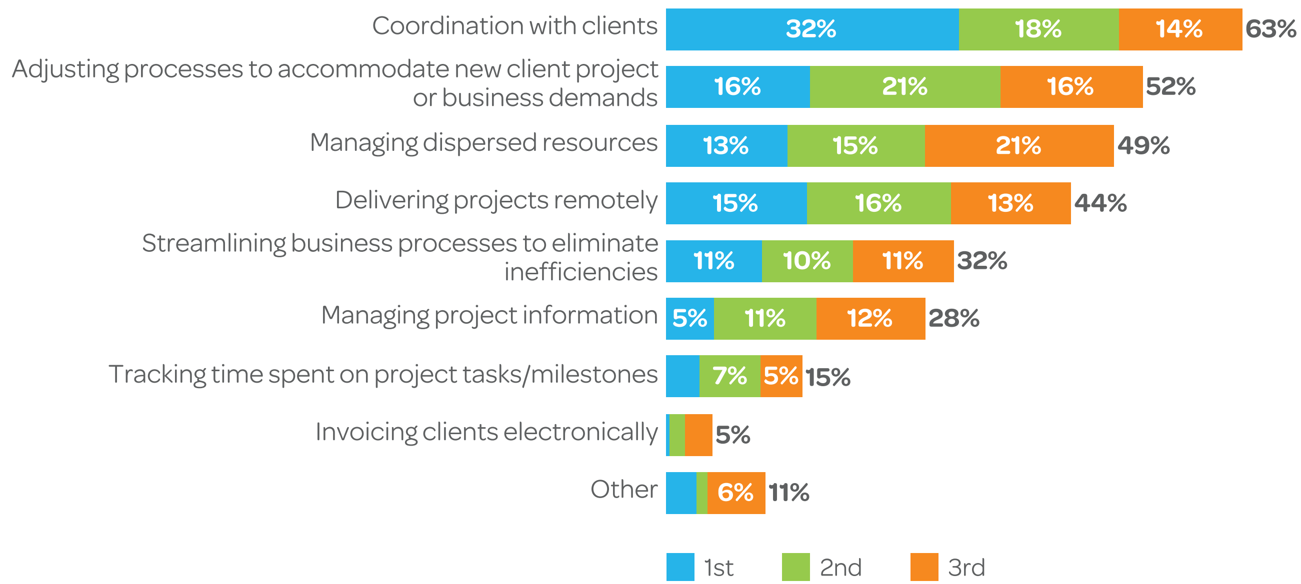
Pandemic Impact: Existing Technologies/Tools

At the outset of the pandemic, many businesses already relied on a broad array of existing technologies and tools, including online meeting platforms, collaboration tools and cybersecurity protocols. The impacts of the pandemic – in particular the rapid rollout of remote working – served to drive rapid incremental investments in these specific areas to shore up near-term security, communication and collaboration capabilities.



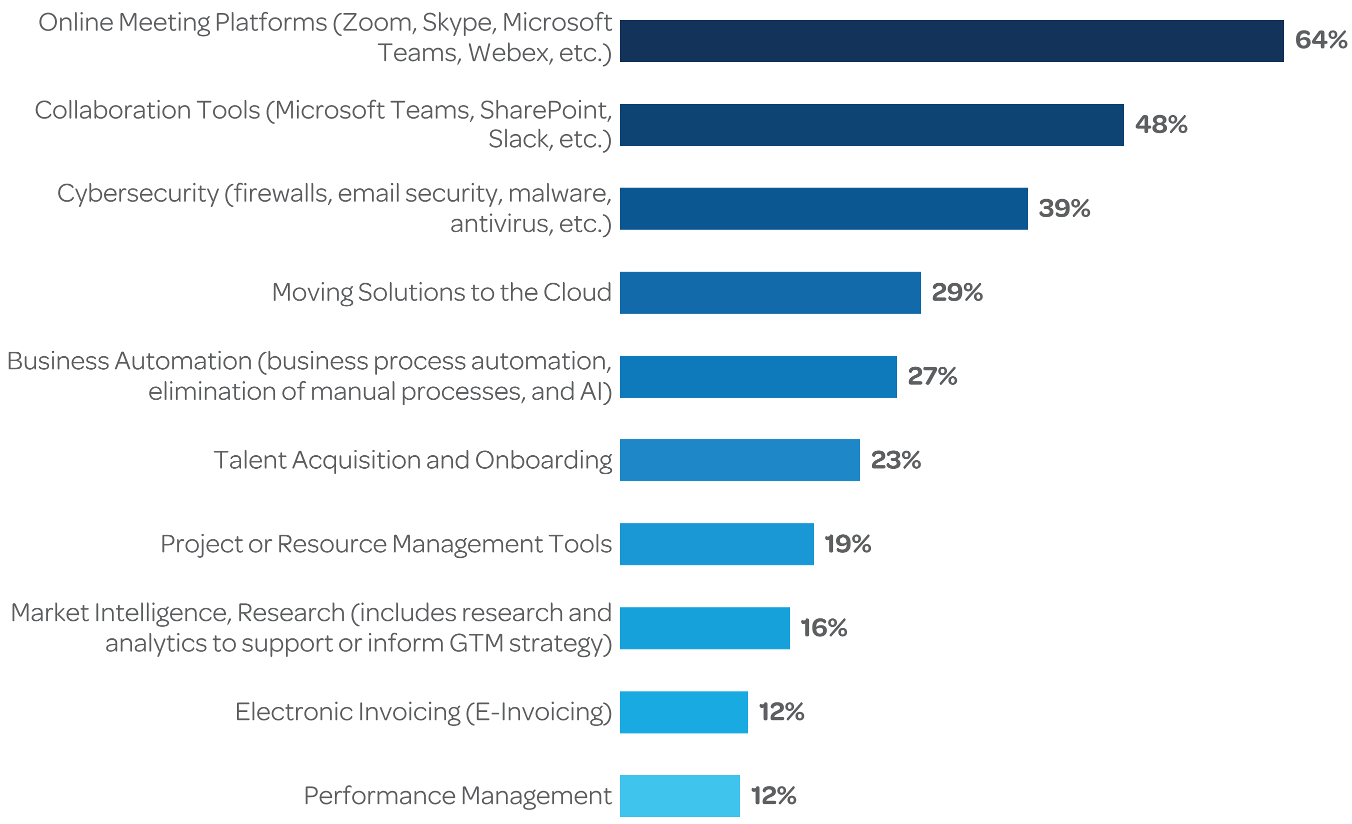
Pandemic Impact: Top Three Challenges

Among the operational challenges presented by the pandemic to businesses of all sizes, the most important was coordination with clients, which was indicated by 63% of respondents. Fifty-two percent (52%) ranked adjusting processes to accommodate new client projects or business demands as number two, followed closely by managing dispersed resources at 49%.



Pandemic Impact:
New Technologies/Tools

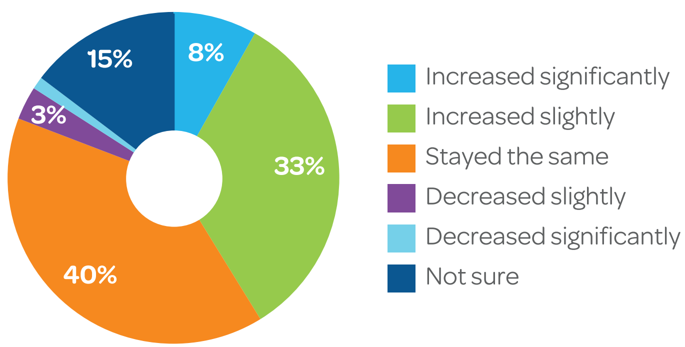
Going forward, businesses expect to increase their investment in their tools and software infrastructure to enhance these new ways of working, including increased cybersecurity capabilities, business automation, project management tools, and moving applications to the cloud. Over the next 12 months, market intelligence to support go-to-market strategies and the business development function and project resource management tools needed are priorities for new investment.



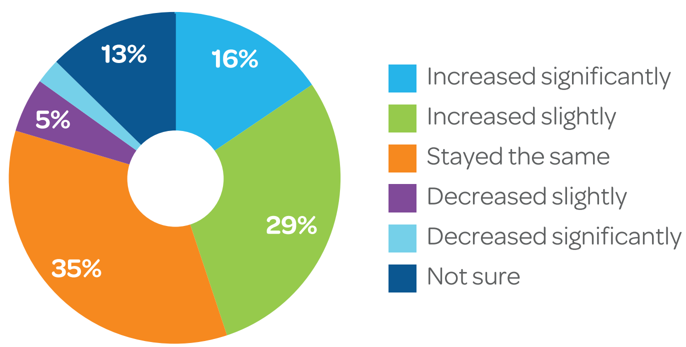
KPI Monitoring

Another development of operating during the pandemic was an increase in the number of key performance indicators (KPIs) monitored by companies, as well as the intensity of focus on those indicators. This is consistent with broader efforts to ensure business continuity, revenue capture and profit optimization in a more difficult operating environment. Forty-five percent (45%) indicated that KPI monitoring increased as business continuity challenges affected companies across the sector. Only 7% reported a decrease in KPI monitoring. At the same time, 41% of respondents indicated that the number of KPIs they measured increased, while only 4% reported a decrease.

Number of KPIs Monitored

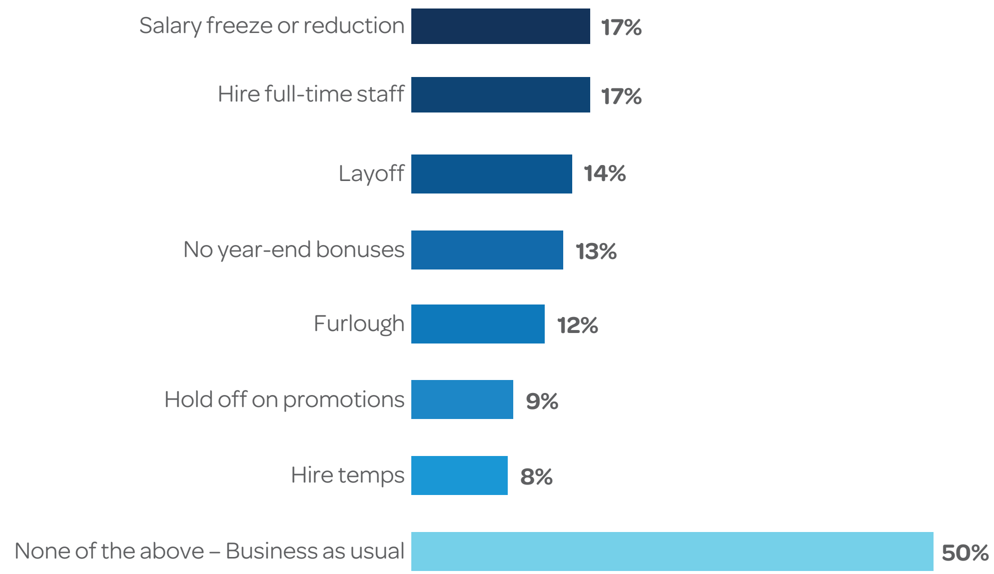


KPI Monitoring



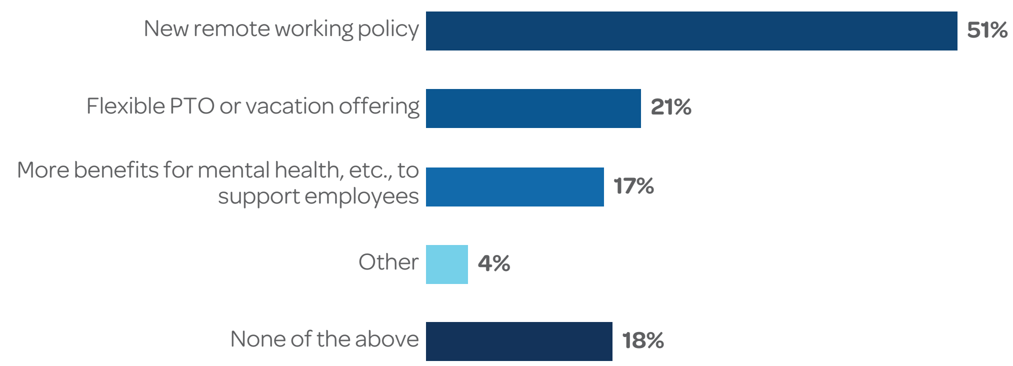
Pandemic Impact: Workforce Adjustment

An important impact of the pandemic was the need by some companies to adjust workforce compensation. While 50% of the Study's respondents reported business as usual with no workforce adjustments, the other half used a variety of methods to keep costs in check, including salary freezes or reductions (17%), layoffs (14%), elimination of year-end bonuses (13%) and furloughs (12%). About 25% of companies increased their workforce with 8% hiring temporary workers and another 17% adding full-time staff.



Pandemic Impact: Employee Benefits

As a result of the more flexible work options necessitated during the pandemic, companies are finding that employee expectations of the ability to work remotely and more flexibly are now engrained. Approximately half of companies in this year's Study plan to adopt new remote working policies, while 70% plan to offer more flexible work options. This is a sea change for the industry, which if implemented will increase competition for talent.



SECTION ONE

Business Development

57%

Businesses of all sizes expect to increase investment in business development over the next 12 months.

Limited business development resources continues to be a top challenge. Fifty-seven percent (57%) of businesses expect to increase investment in business development in 2021, with large businesses planning the biggest increase.

At the time of the 2019 Study, the COVID-19 pandemic was just beginning to surface and had not yet affected enthusiasm regarding 2020; expected results remained high. Once the full impact of the pandemic took hold, it disrupted established ways of operating and forced companies to adapt quickly.

One of the major challenges companies faced in 2020 was making the most of limited business development resources and retaining top talent. Companies had to adapt to an environment where face-to-face events, such as conferences, trade shows and networking opportunities, were halted. This made selling and finding teaming partners more challenging. In response, companies stepped up their reliance on proactively supporting business development staff with marketing-generated leads and market intelligence databases. Active client relationships were more important than ever, as were established teaming partners.

TOP THREE BUSINESS DEVELOPMENT CHALLENGES

1. Limited business development resources
2. Increased competition
3. Creating opportunity pipeline forecasts and reports

The competition for new business was robust despite an overall flat win rate. Small and medium-sized businesses won 33% of competitive proposals they submitted, while large companies were successful in 48% of competitive proposals submitted, demonstrating that size and scale were a significant competitive advantage. Average dollar values for submitted proposals, however, dropped from $145 million to $94 million year over year. With reduced proposal value, companies appear to be seeking more diversity in their client mix and seem less reliant on a small number of clients. Revenue generated from top three clients fell to 62% versus 75% a year ago.

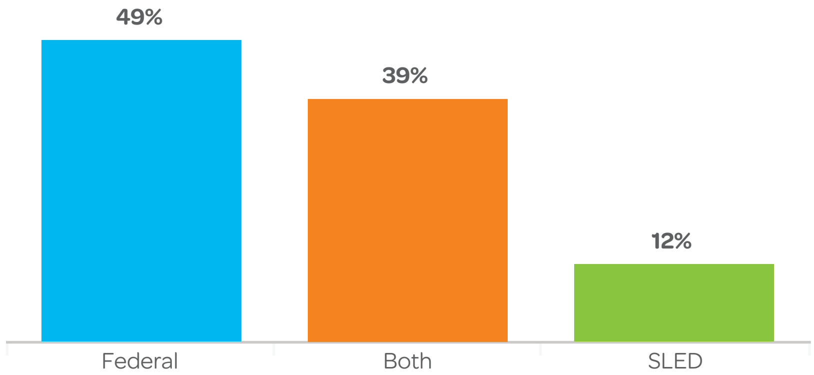
In an environment of new working models, the ability to successfully track pipeline opportunities and forecasts was somewhat impeded. As these indicators are key to predicting and winning future sales, business development professionals will need to turn a sharp focus to this area in 2021.

Companies are looking toward better opportunity identification and expansion into new business areas for growth going forward.

Areas of Government Business

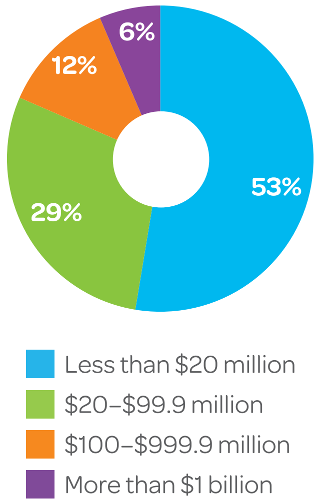
Companies that do business with the federal government accounted for 88% of respondents to the 2020 Study, a decrease from 93% in 2019. Those engaged in both federal and SLED market categories accounted for 39% of respondents, a slight uptick versus last year. Engagement in both markets provides a wide base of opportunities, but also generates increased complexity for managers complying with varying regulations and relationships.

The representation of companies that only do business in the SLED market grew from 7% to 12% in 2020, an increase of five percentage points. The increase seen in 2020 may be attributable to the perception that state and local governments will be investing in upgrades to many legacy systems to handle growing data needs, migration to the cloud, remote working infrastructure and cybersecurity. The expectation that government stimulus would support these functions contributes to the sector's increasing appeal.



Respondents by Government Business Revenue Size

In this year's study, small companies represented 53% of respondents, up from 48% in 2019. Medium-sized companies comprised 29% of respondents, up from 24% in the previous year. Respondents from large businesses decreased to 18% versus 27% the prior year.

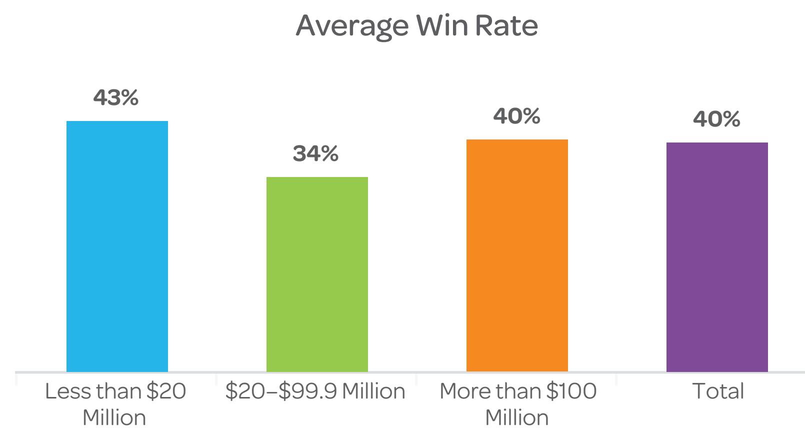


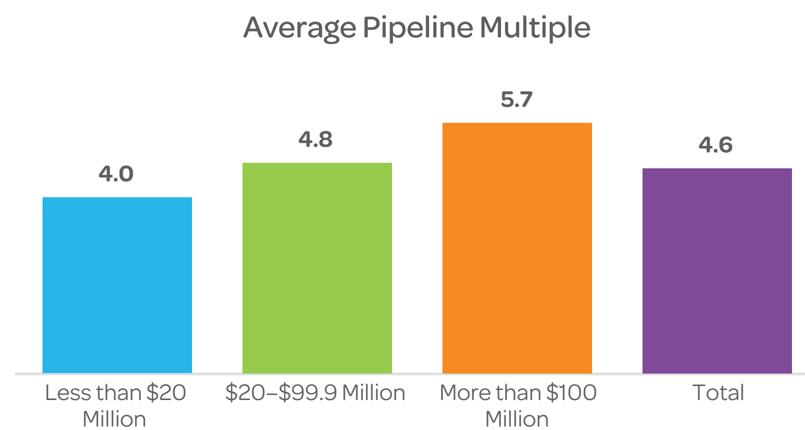
Win Rate and Pipeline Multiple

The overall win rate reported by 2020 Study respondents was flat year over year at 40%, with small businesses indicating a three percentage point increase while large businesses reported a five percentage point decline. Medium-sized businesses remained relatively flat at 34%. Both the average and median win rate reported stayed the same at 40% and 35%, respectively. The rate of proposals awarded is highest for large businesses, demonstrating that the value of contracts won provides leverage beyond its specific win rate.

A company's win rate is affected by how aggressive companies are in seeking new business. For example, a company that bids only in "safe" situations where it is likely to win may have a high win rate but could be overlooking new business opportunities and limiting itself to a lower base of possibilities. A conservative approach to bidding may result in a win rate that looks successful but fails to achieve the growth available. Conversely, the choice to bid on opportunities that are speculative decreases the win rate and may squander business development resources. It is essential, therefore, that companies evaluate which bids to pursue with an objective assessment of their likelihood of success.

The average pipeline multiple needed to achieve sales objectives remained largely flat year over year in 2020. Large businesses experienced the largest increase to 5.7 compared with 4.0 the previous year. This may reflect declining contract values. The multiple for small businesses decreased to 4.0 from 4.7 the year prior.



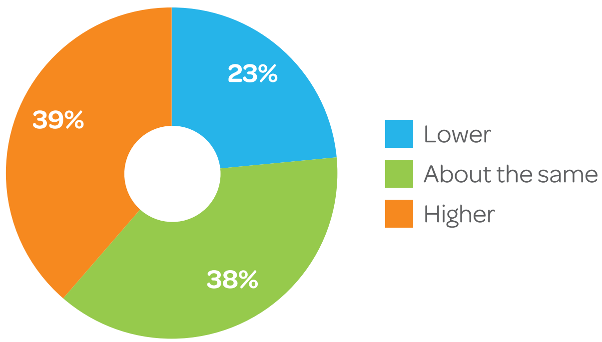


Sales in Government Markets

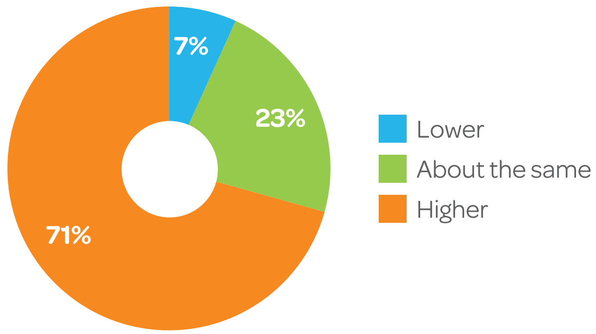
Responses to this year's Study showed that government contracting revenues declined on a year-over-year basis. Twenty-three percent (23%) of participants indicated lower revenues in fiscal year 2020. Fewer companies indicated that revenues grew or stayed the same.

Over 70% of Study respondents expect revenues to increase in 2021. Twenty-three percent (23%) look for revenues to be about the same as in 2020, while only 7% expect revenues to be lower. Reasons for this optimistic outlook include impending control of the pandemic, the recently completed presidential administration change, and the ability of government agencies to return their attention to fundamental activities and away from COVID-19.

Past Year's Government Market Sales

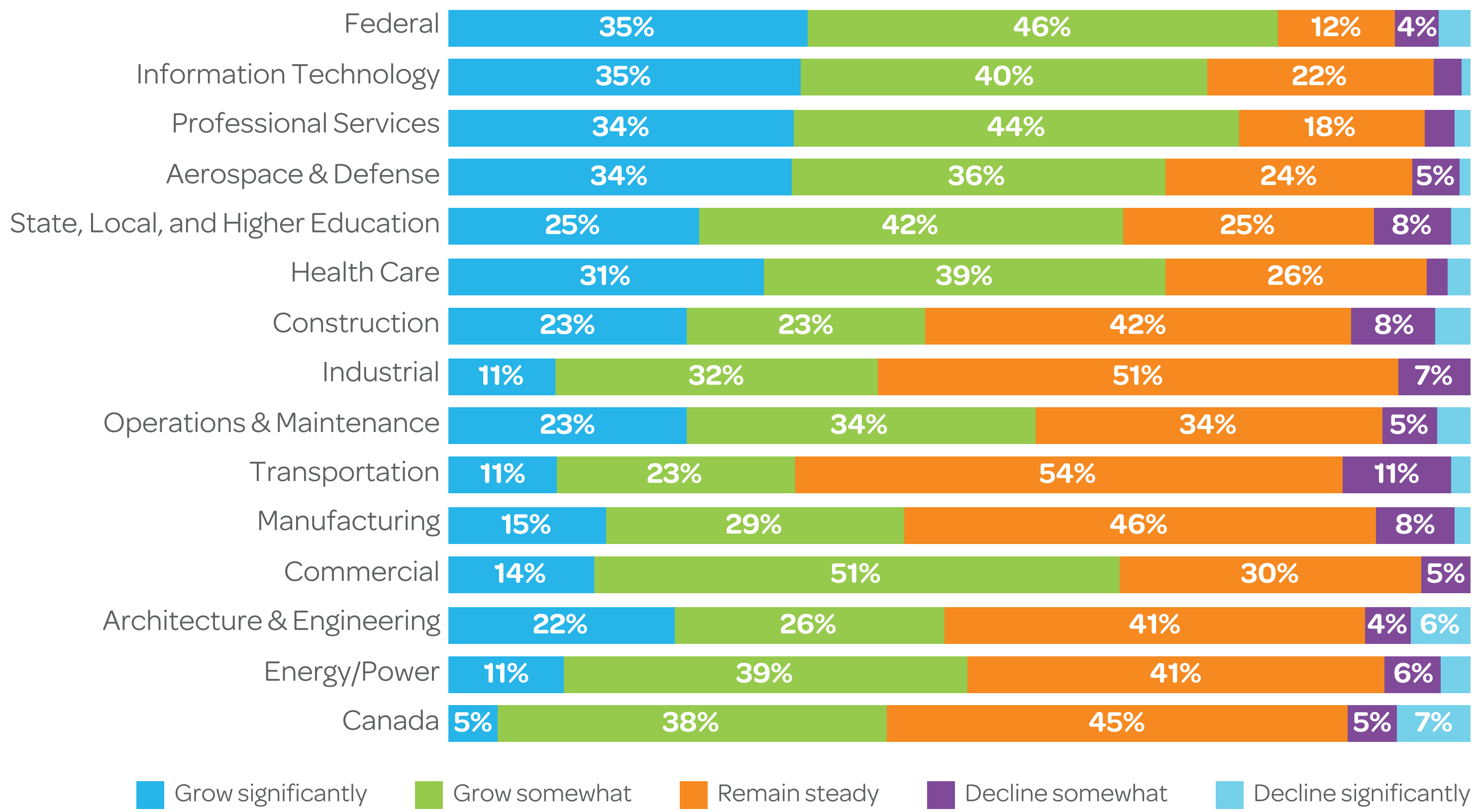


Next Year's Government Market Sales



Expected Position in Industries

Companies expect significant growth in the next 18 months, with particular emphasis on the professional services, aerospace and defense, health care, and architecture and engineering industries. SLED markets expect to benefit from the recently enacted stimulus. Seventy-five percent (75%) of respondents look for IT business to either grow significantly or somewhat. The outlook for every sector is positive.



Top Business Development Challenges

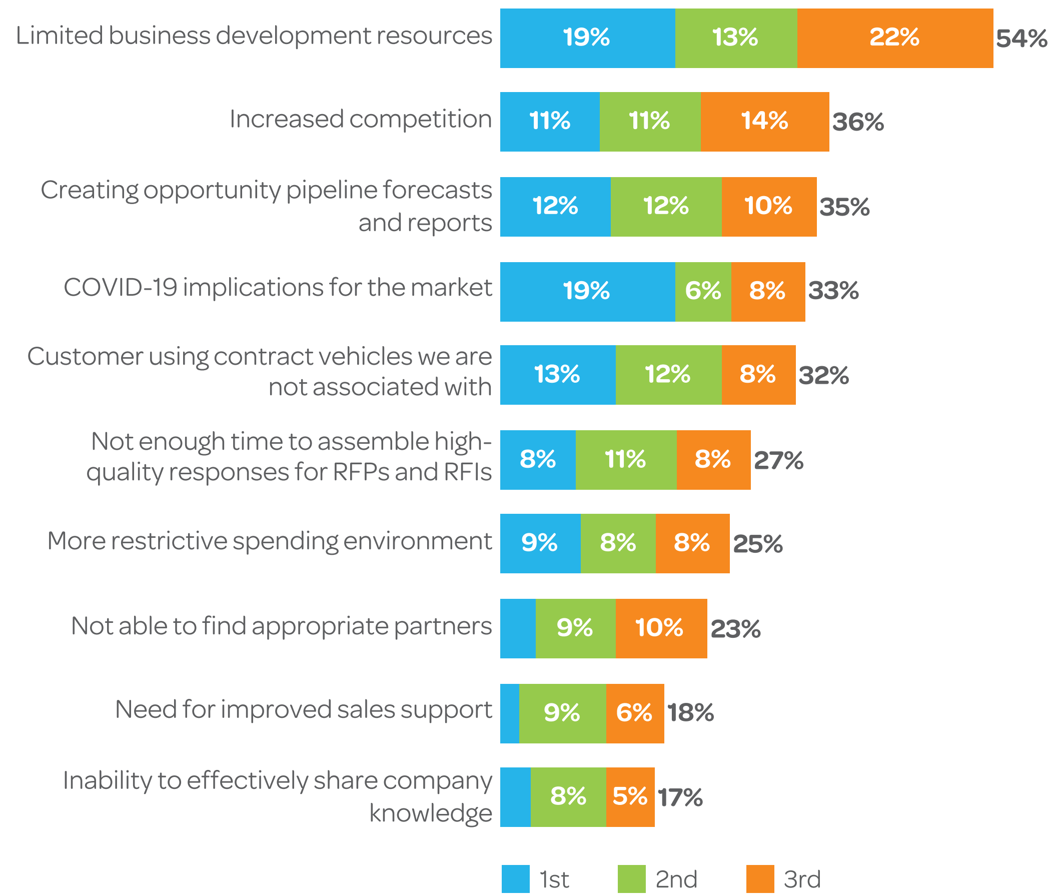
Business development professionals had a new challenge in 2020, which was to assess and deal with the ramifications of the COVID-19 pandemic. Normal ways of doing business were upended, and the need to do more with fewer resources grew ever more important.

The usual methods of developing new opportunities through networking and in-person events were curtailed, resulting in difficulty finding appropriate partners, trouble creating high-quality responses to requests for proposals (RFPs) and requests for information (RFIs) and an inability to share company knowledge. This all occurred against a backdrop of increased competition and a government spending environment that attracted many new entrants.

Going forward, it is unclear when the pandemic response will permit a return to in-person business operations. Companies therefore must continue to adapt business development activities to this different environment.

As resources continue to be limited, businesses should rethink how best to use their capabilities and people. For example, strong existing customer relationships and deep experience with the government contracting world will be highly valued.

It will be more important than ever to recruit and retain top talent who are able to pivot nimbly as conditions change and hit the ground running when hired.



70%

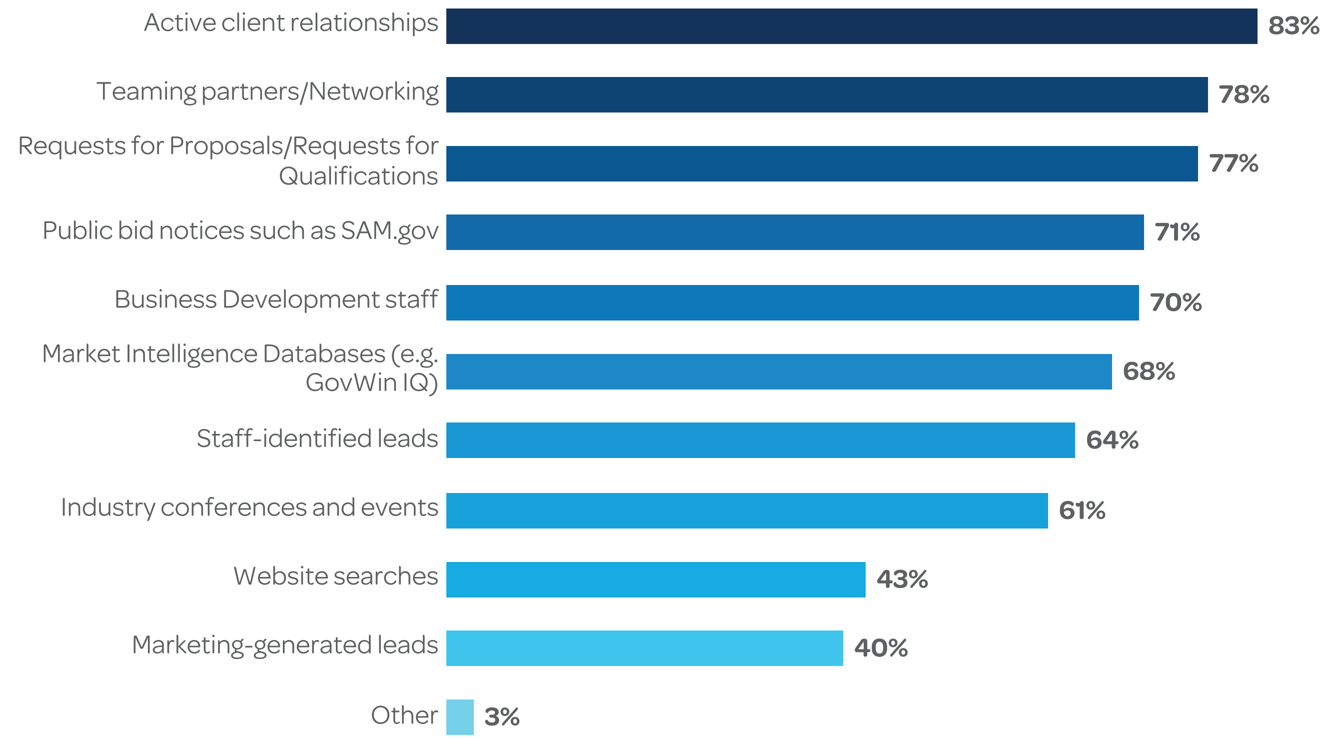
Believe government sales will increase in 2021

Significant growth is expected in professional services, aerospace and defense, health care, and architecture, engineering and construction (AEC).

Sources to Identify New Opportunities

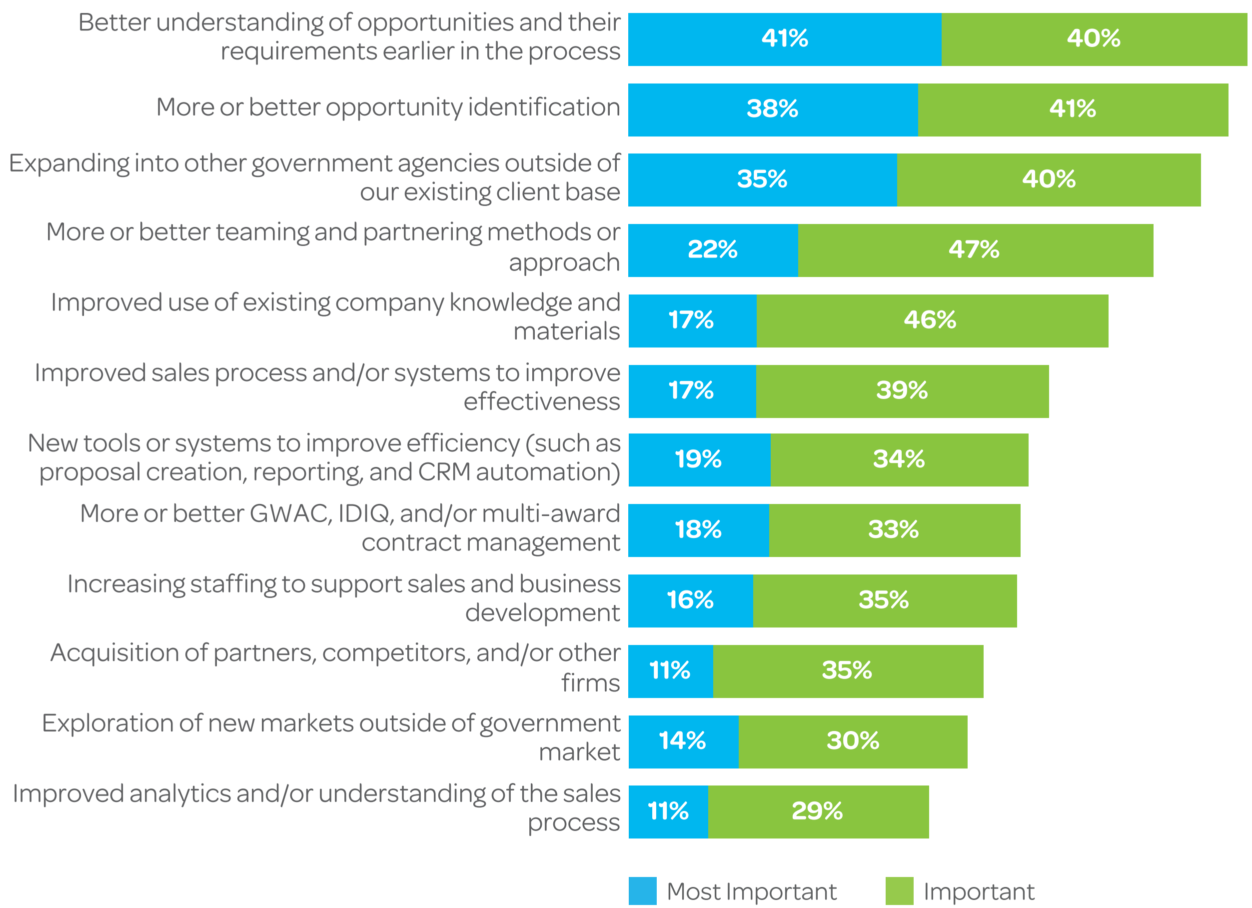
Identification of new pipeline opportunities focused on active client relationships, teaming partners/networking, and RFPs/RFQs (requests for quotes). In 2020 business development professionals lost the opportunity to use in-person events, such as conferences and trade shows, to develop new leads. Marketing-generated leads offset the decrease, while more professionals took advantage of market intelligence databases like GovWin IQ to uncover new opportunities.

Going forward, companies will have to continue to learn how to team in a virtual world. Some may decide that the costs in time and money to reprise an active face-to-face schedule may not be the best use of resources. Some resetting of business development approaches will certainly occur, with differing approaches by varying sizes of companies.



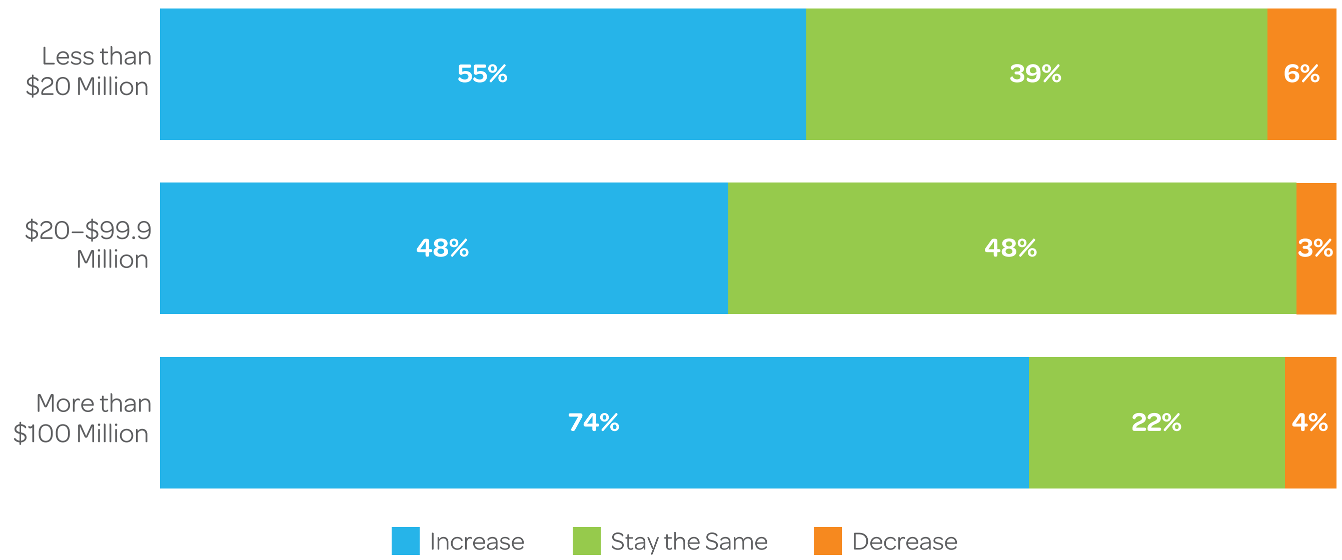
Addressing Top Business Development Challenges

The top three initiatives cited by respondents in addressing top business challenges remained unchanged for 2020. There was a continued focus on better understanding of opportunities and their requirements earlier in the process, more or better opportunity identification, and expanding into other government agencies outside of our existing client base. To achieve those objectives, better tools and systems are required to improve efficiency and increase the ability to identify new market developments. Better teaming and partnering approaches will more effectively utilize the resources that are likely to remain somewhat constrained in 2021.



Expected Investment in Business Development

Dropping in importance (-12%) was a focus on increasing staffing to support sales and business development. Businesses are looking to turn this around in 2021 with 57% of businesses expecting to increase investment in business development over the next 12 months. This was led by large businesses with 74% expecting to increase investment.



CLARITY OUTLOOK

Business Development

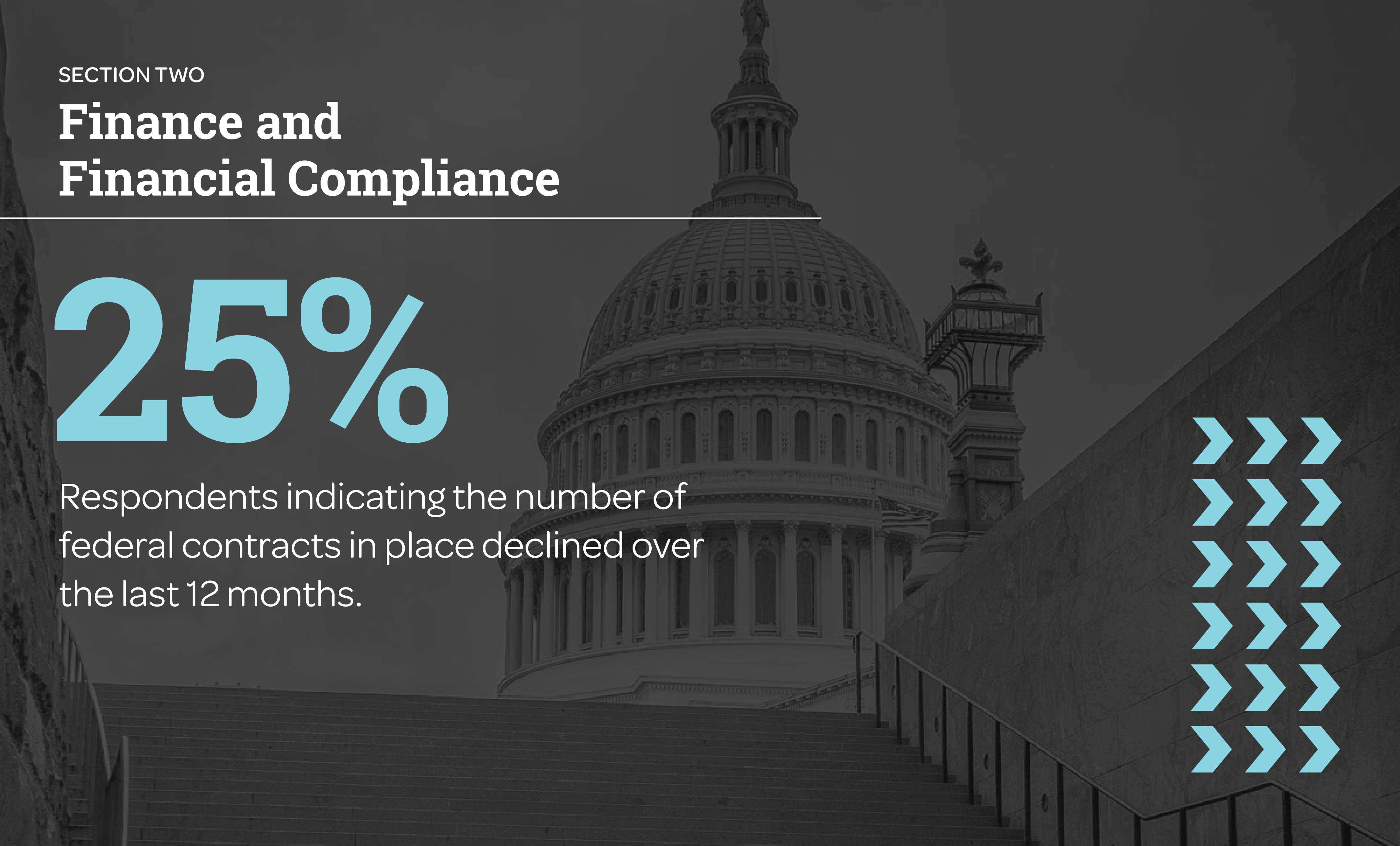
2020 challenged companies to make the most of limited business development resources in an environment where the tried-and-true tactics were often no longer available. New ways of connecting with customers could be here to stay.

The need to be more efficient in a challenging environment of limited resources is the overarching theme of business development today. Among the ways to accomplish this include updating how teaming partners are selected to maximize the mix of capabilities offered and to expand market coverage. Investment in tools to maximize revenue and profit from existing contracts and prospects will further stretch capabilities, while continuing to pivot toward new ways to extend market reach.

The outlook is bright as businesses expect to increase investment in business development and tighten their focus on working smart. It is more important than ever that companies succeed in their competition for talent and help existing employees find new approaches to old problems.

SECTION TWO

Finance and Financial Compliance



25%

Respondents indicating the number of federal contracts in place declined over the last 12 months.

Growth projections made in 2019 for 2020 were robust and optimistic, but the pandemic presented businesses with new challenges that pressured their results. Large businesses were more likely to continue on a "business as usual" basis, while many smaller businesses were not able to do so. As the focus turned to fundamentals and achieving business continuity, companies also focused on getting smarter about financial execution. Process optimization and managing risk were a highlight of efforts in 2020, given the likelihood of a near-term impact to financial results.

On a year over year basis, financial challenges cited by Study participants were not radically different, but the need for predictability in financial performance grew sharply in importance. Understanding and implementing new compliance requirements also took on higher importance so that businesses could avoid regulatory challenges and anticipate audit requirements.

TOP THREE FINANCIAL CHALLENGES

1. Increasing profitability
2. Achieving organic topline growth
3. Predictability of financial performance

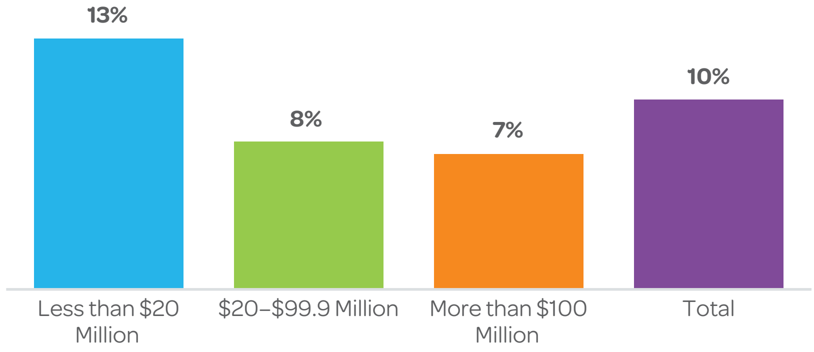
Companies appear to be increasing their focus on driving greater diversification – with a distinct emphasis on driving market penetration, achieving greater product line breadth, and building an increasingly-diverse customer base. This diversification is imperative to offset any lingering effects of the pandemic and put companies on the path to achieving higher growth rates in 2021.

Fundamentals were the focus in 2020 as businesses adapted to the pandemic's effects.

Profitability

Among Study participants, average profit margin declined significantly in 2020, with all sizes of companies reporting lower results. Small businesses were particularly affected, with the margin decreasing 32% year over year.

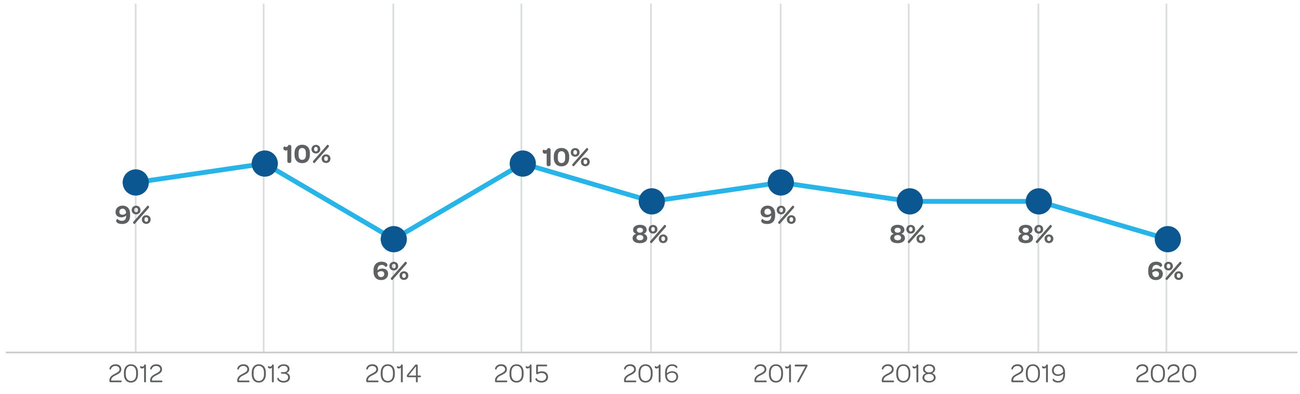
Average Profit Margin



Nine-Year Trend

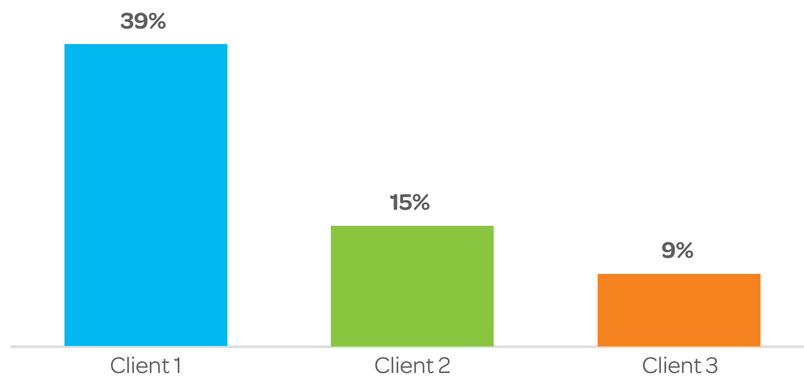
Median profit margin declined to a level not observed since federal budget sequestration occurred in 2014. Since then, businesses had reported a consistent annual trend of 8% to 9% which fell in 2020 to 6%.

Median Profit Margin: Nine-Year Trend



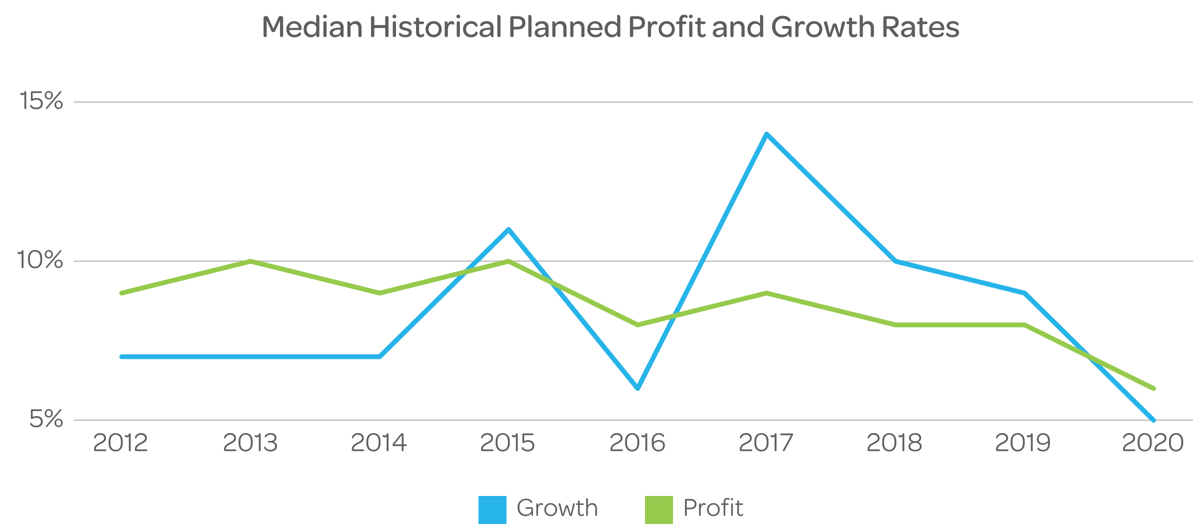
Average Revenue from Top Three Clients

Businesses reported a greater distribution of revenues over their client bases in 2020, as their dependence on their top three customers declined. This was likely driven by agencies focused on pandemic response and affected both current project evaluation and the pace of new contract awards. In order to protect these revenue streams, companies appear to have sought a greater diversity in clients during the downturn. As the environment fluctuated throughout 2020, companies sought to reposition themselves. While still heavily reliant on a limited number of customers, the net revenue represented by companies' top three customers was down to 62% in 2020 versus 75% a year ago.



Growth

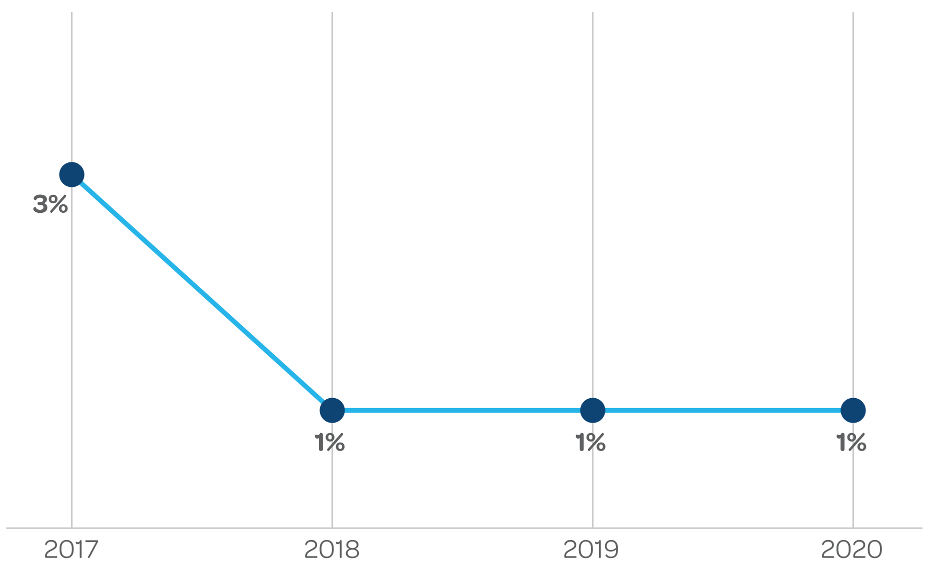
Business continuity challenges stemming from the pandemic's impact affected projected growth rates in 2020 compared with 2019. Median planned growth has continued to slow since 2017 from a high of 14% to 5% in 2020. Profits followed suit, decreasing from a high of 10% in 2013 to 6% in 2020.



Costs

Increases in average unallowable cost rates affected small businesses disproportionately in 2020, where their percentage of unallowable costs increased three-fold. For small companies, the costs of bidding and proposals jumped 43% versus a year ago, while medium-sized and large companies reported no material changes relative to 2019. On a trended basis, the median unallowable cost rate has remained flat since 2018, when it decreased from 3% in 2017.

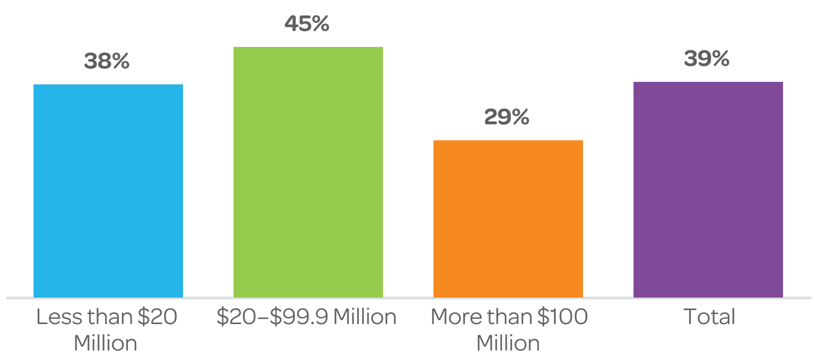
Median Unallowable Cost Rate: Four-Year Trend



Overhead Rates

Overhead rates have increased since 2019, as a shift in medium-sized and large businesses' rates raised the average overall composite overhead rate by three percentage points. Medium-sized businesses had the largest increase, rising from 30% to 45%, the result of a 10% rise in fringe rates.

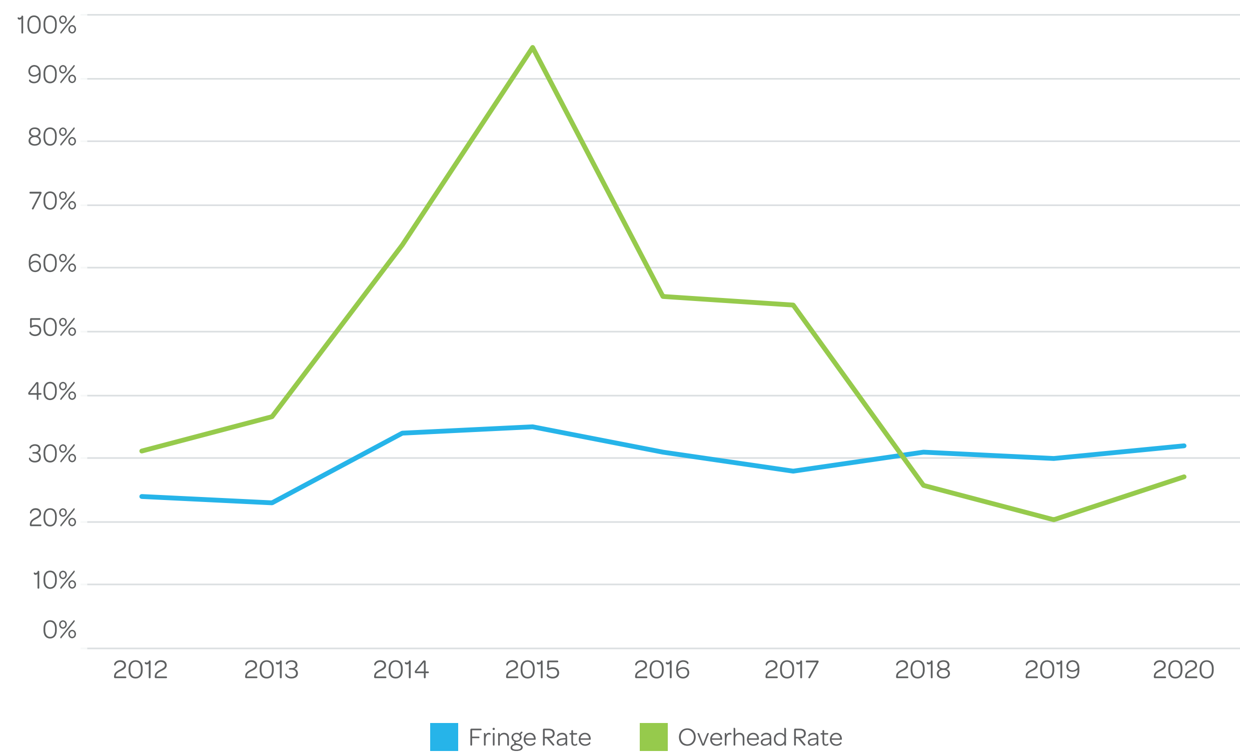
Average Overall Composite Overhead Rate



Nine-Year Trend

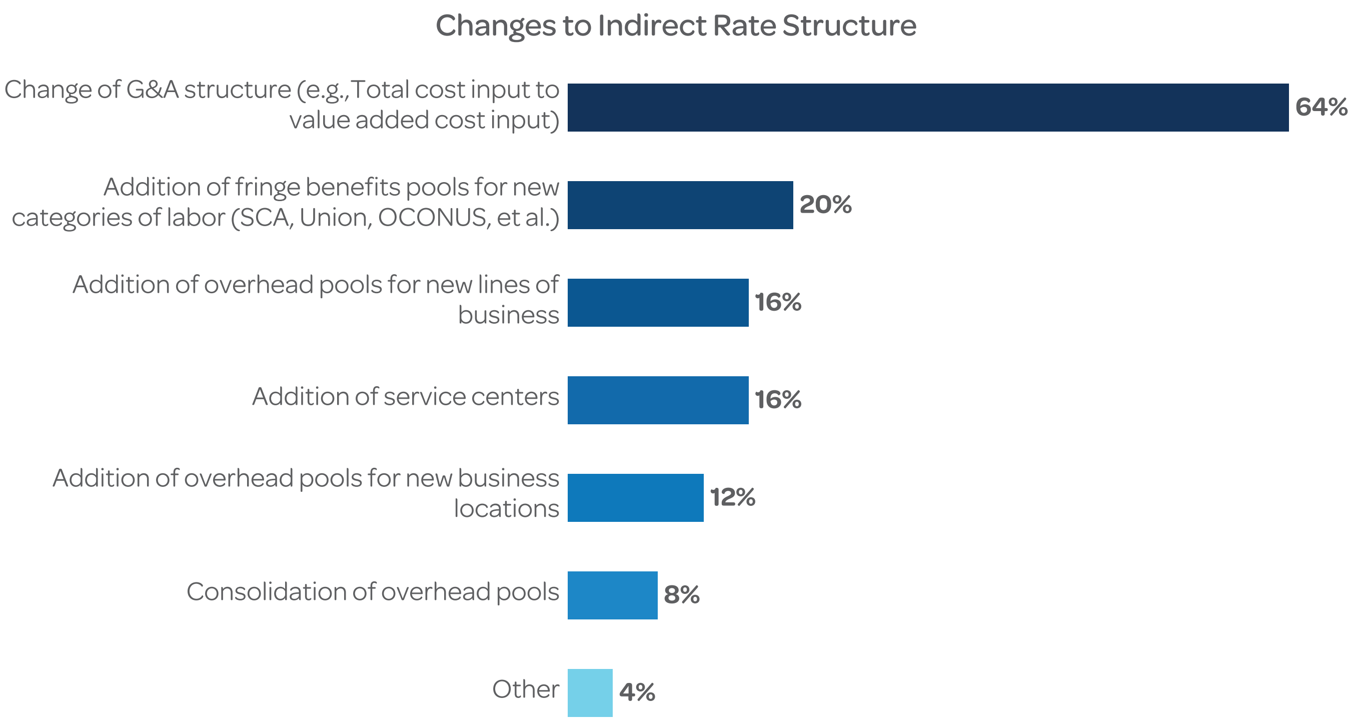
Median fringe rate has remained largely steady over the last three years. In the nine-year trend since 2012, the fringe rate has increased to 32% in 2020 from 24% in 2012. Despite a spike in 2015, median overhead rate was also largely unchanged over the last three years, finishing 2020 at 20%, up five percentage points over 2019 and up one percentage point versus 2018.

Median Fringe and Overhead Rates: Nine-Year Trend



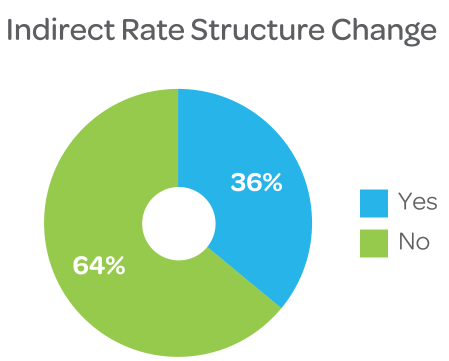
Indirect Rate Structure

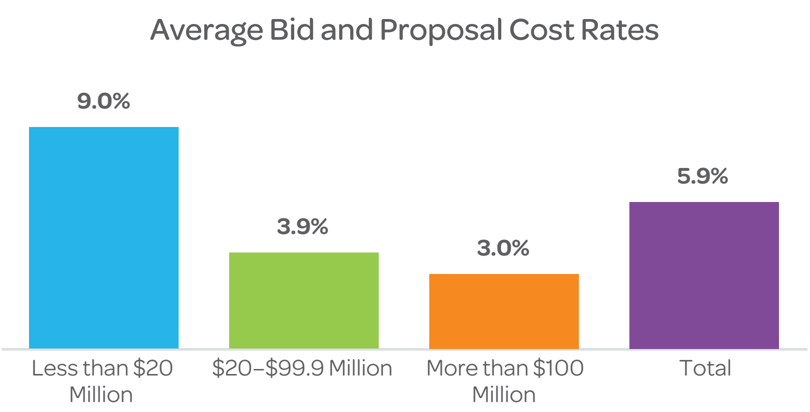
Among the 36% of companies who experienced a change in indirect rate structure in the last two years, general and administrative (G&A) cost structure was identified as a key driver of the change. Other significant drivers included the addition of fringe benefit pools for new categories of labor and the addition of overhead pools for new lines of business.



Bid and Proposal Costs

Average bid and proposal cost rates increased one percentage point in fiscal 2020. Small businesses in particular saw a dramatic change in reported costs compared with the prior year, experiencing an increase of 43% in the period. As smaller businesses continue to focus on becoming more lean and efficient, this will continue to be a particular area of focus.

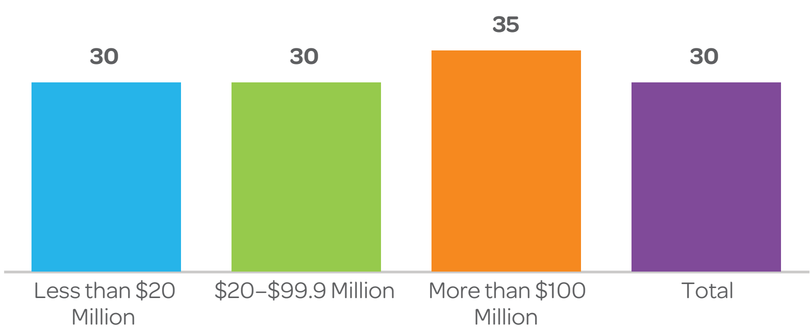




Nine-Year Trend

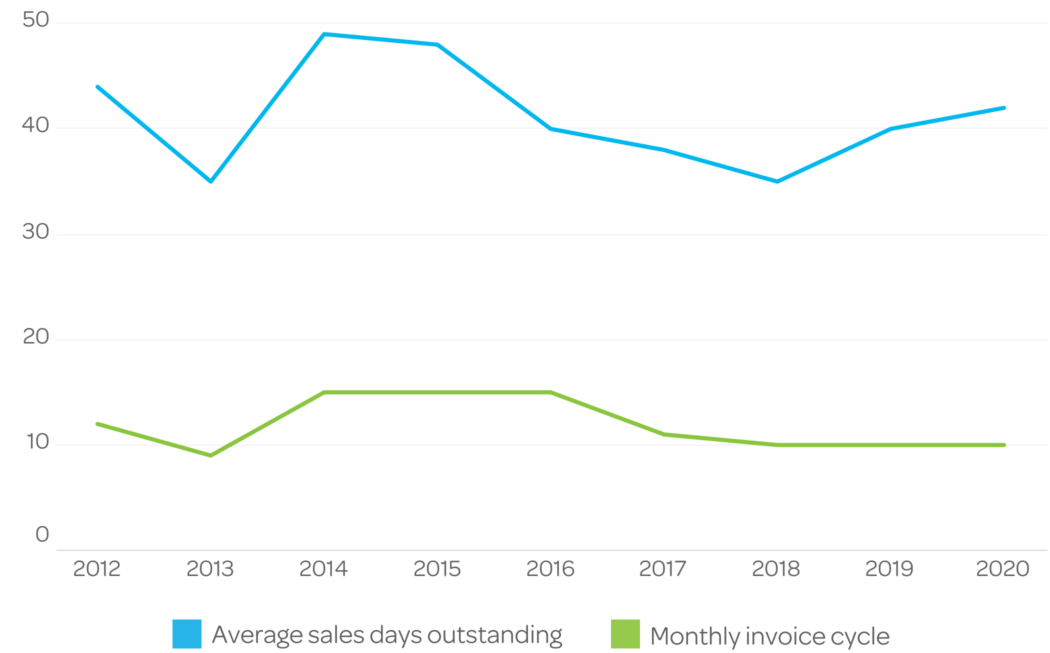
Average Days Sales Outstanding (DSO) and monthly invoice cycles have fluctuated over the last nine years. Average DSO has ranged from 35 to 49 days, with the high registering in 2014. Monthly invoice cycle, which is measured from the end of the billing cycle to invoice submission, has also varied between nine and fifteen days during the period. Results in 2020 indicate a continuation of the near-term trend, with average monthly invoice cycles at 10 days.

Median Days Payable Outstanding (DPO)



Receivables collection, represented by median days payable outstanding (DPO) was 30 days in 2020, with large businesses accounting for a slightly longer payment period than those reported by small or medium-sized businesses.

Average Days Sales Outstanding and Monthly Invoice Cycle: Nine-Year Trend



10%

A significant decline in profitability hit small businesses particularly hard.

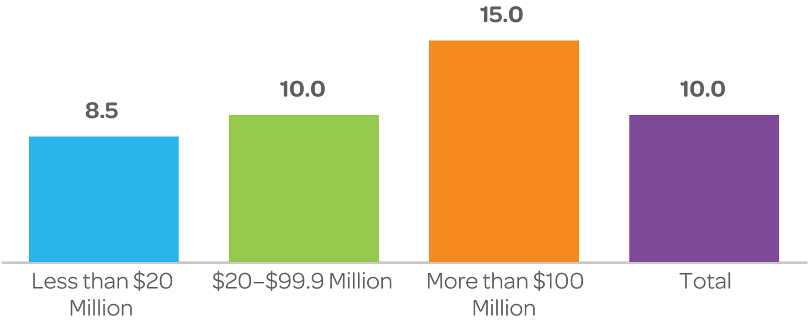
In fiscal year 2020, average profit margin declined from 15% to 10% as the pandemic disrupted business operations.

Factors that Influence Cash Flow

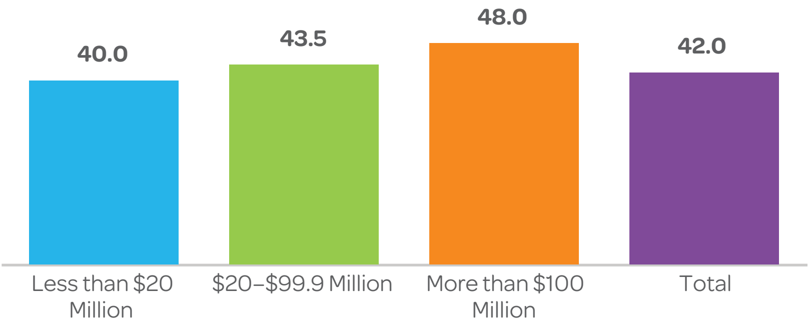
In 2020, while companies directed their principal attention to business continuity rather than maximizing cash flow, they managed to maintain consistent cash flow performance. The average monthly invoice cycle remained largely unchanged year over year, with businesses invoicing at roughly 10 days overall. However, small differences in invoicing and collections – like the slight increase of two days among medium-sized businesses in 2020 – can be critical to maintaining an acceptable cash flow.

Median DSO increased by two days or 5% in 2020. Increases in DSO in 2020 squeezed the liquidity of medium-sized and large businesses during the pandemic with small businesses holding steady.

Average Monthly Invoice Cycle



Median Days Sales Outstanding



Federal Contract Trends

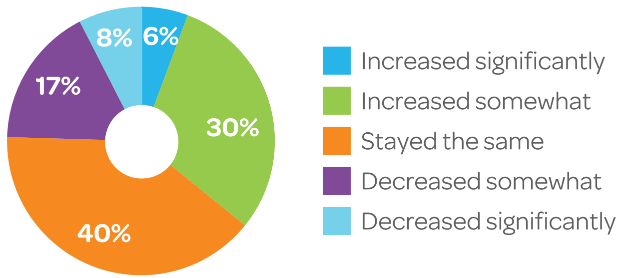
In the last 12 months, there was a greater amount of volatility in the number of federal contracts awarded, with 25% of respondents indicating a decrease in active federal contracts compared with 17% a year ago. Contract awards likely were affected by delays driven by the COVID-19 pandemic and a potential change in presidential administrations.

Small businesses were particularly vulnerable due to a greater risk exposure given access to fewer contract vehicles and less financial cushion than their larger peers, underscoring the reality that for many it was a year of feast or famine when viewing the industry at a segment level.

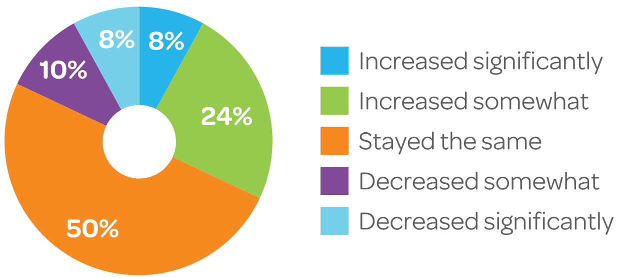
Change in IDIQ Revenue

Revenues from indefinite delivery, indefinite quantity (IDIQ) contract vehicles decreased along with other federal contracts in 2020. Fifty percent (50%) of respondents indicated revenues from these contract types had remained unchanged since 2019, while 18% experienced a decrease versus a year ago. The lion's share of changes were experienced among small and medium-sized businesses – with more reporting declines – while large businesses remained largely unchanged with respect to IDIQ contract revenue.

Change in Federal Contracts

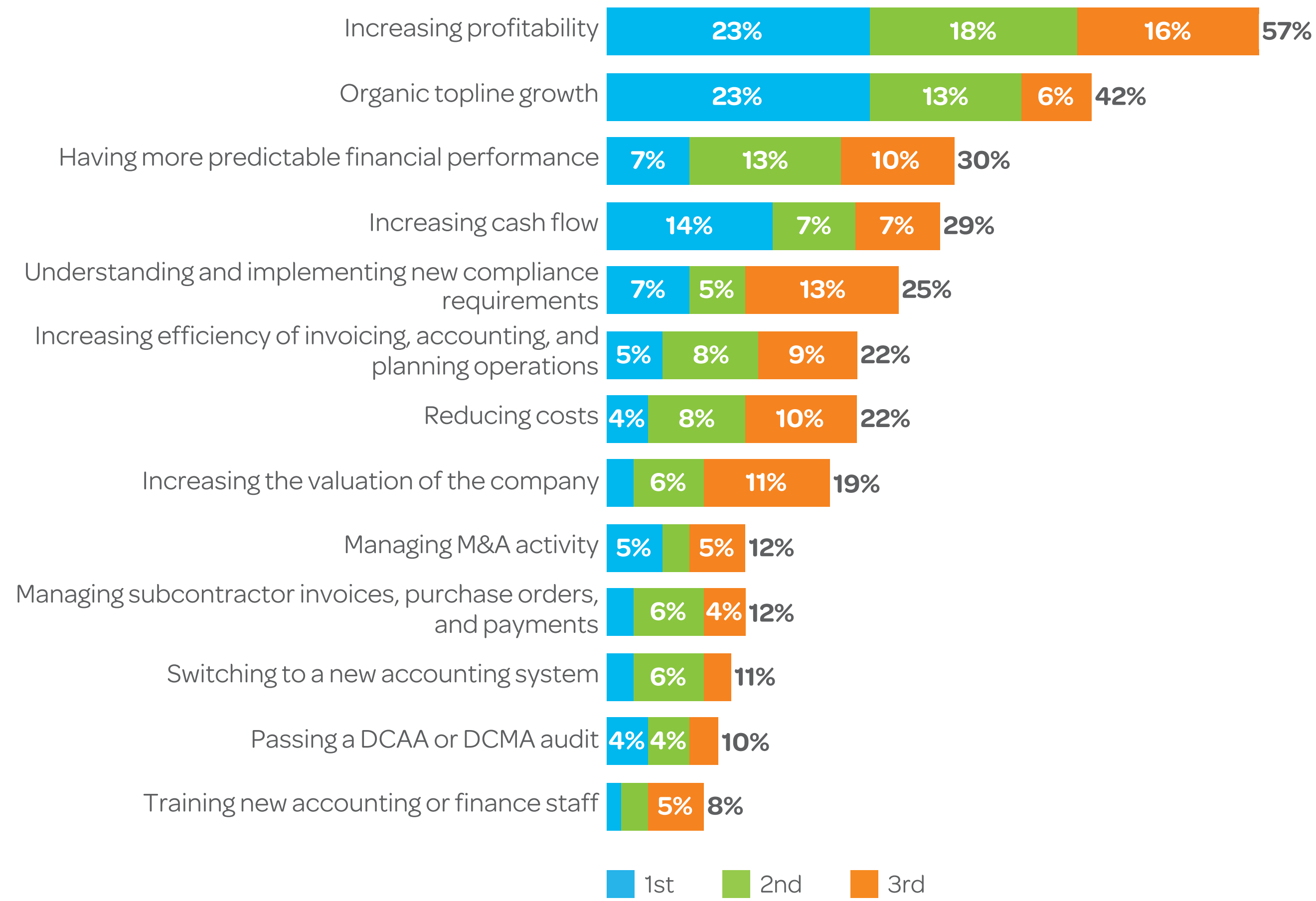


Change in IDIQ Revenue



Top Financial Challenges

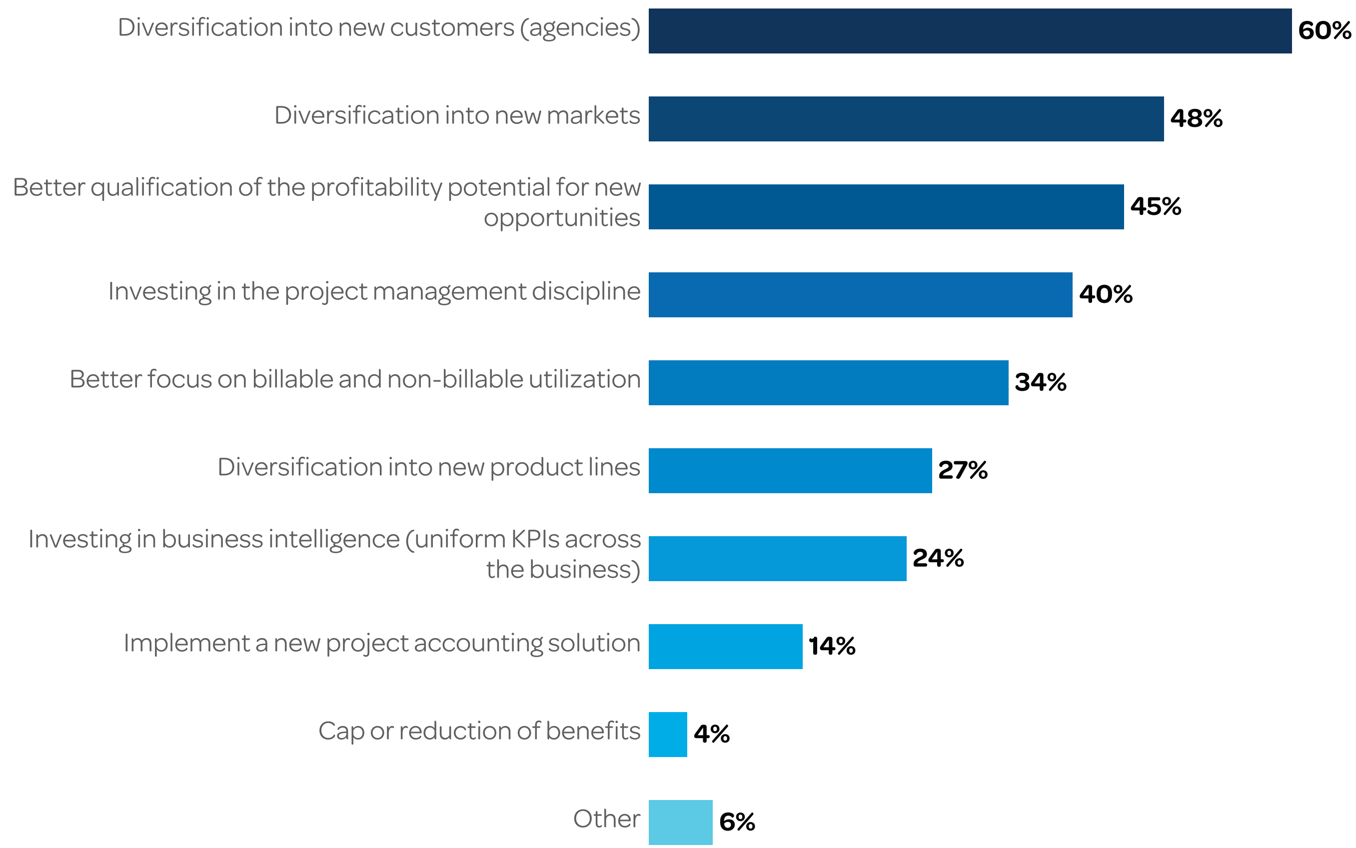
Respondents to this year's Study faced numerous financial challenges. In addition to the top three – increasing profitability, organic topline growth and having more predictable financial performance – companies sought out opportunities to improve efficiency and avoid regulatory hurdles. Understanding and implementing new compliance requirements was called out by 25% of respondents, up from 16% in 2019. Increasing the efficiency of invoicing, accounting and planning operations remained an area of focus, although less so than 2020. As business recovers in 2021, it is expected that investment in productivity and efficiency tools will help unlock greater profitability.



Addressing Top Financial Challenges

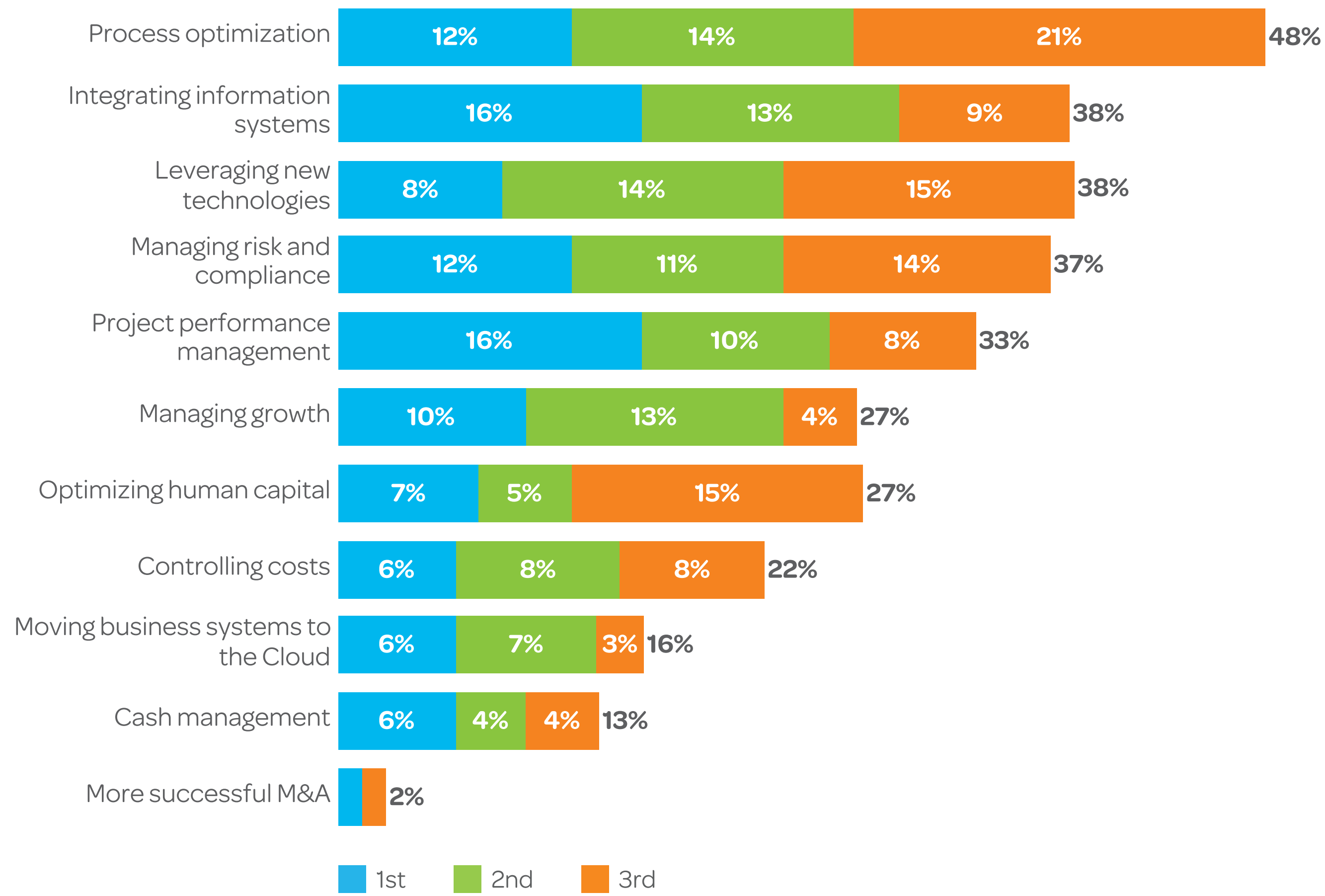
Diversification was cited as a key focus in addressing recent financial challenges, with indications that businesses are focused on acquiring new customers (agencies), gaining access to new markets and offering new product lines to their customers. Recognition from respondents that better qualification of the profitability potential of new opportunities (48%) reflects businesses' realization that growing the top line alone is not sufficient to drive successful growth.

Investment in business intelligence to achieve uniform KPIs across the business was a focus for 24% of respondents, highlighting the need to bring careful analysis to the business and facilitate necessary changes.



Top Digital Financial Transformation Challenge

In 2020, process optimization replaced controlling costs as the top challenge to digital transformation as businesses altered their focus on driving profitability and business predictability. Also near the top of this year's list of challenges was managing risk and compliance, while optimizing human capital became less of a pertinent focus. Integrating information systems rose in emphasis, as did moving systems to the cloud.



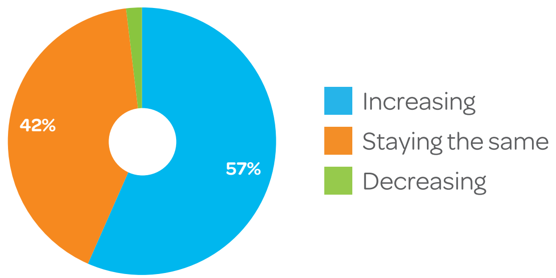
Compliance

Compliance with existing and new government regulations is both expensive for companies and crucial to their success. The ratio of 2020 respondents that expect compliance costs to increase over the next 12 months was higher, with 57% expecting higher costs and 42% looking for costs to remain stable, results that were roughly reflective across business size segments.

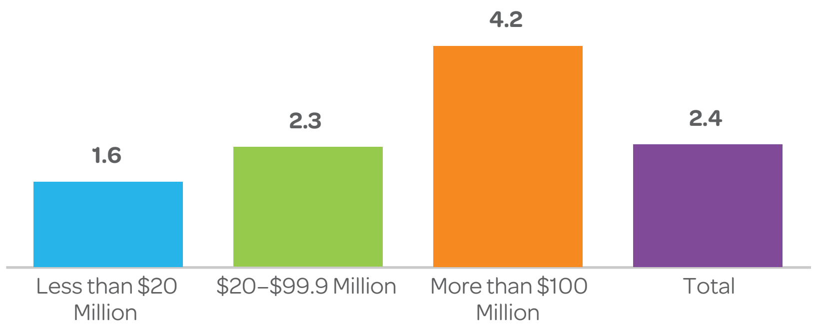
Overall, audit volume in fiscal year 2020 was roughly equivalent to the prior year. Each size of business experienced a similar level of oversight as a year ago. Many companies are trying to improve their preparedness by performing internal audits, periodically reviewing financial transactions and project schedules to enhance compliance likelihood ahead of official government audits.

When it comes to dedicating time preparing for government audits, small businesses indicated the least time spent, while large businesses spent the most time preparing, likely the result of the size, scope and complexity of those engagements. Qualitatively, it appears companies have increased headcount in their compliance organizations, a reflection of the importance of these activities to their underlying businesses.

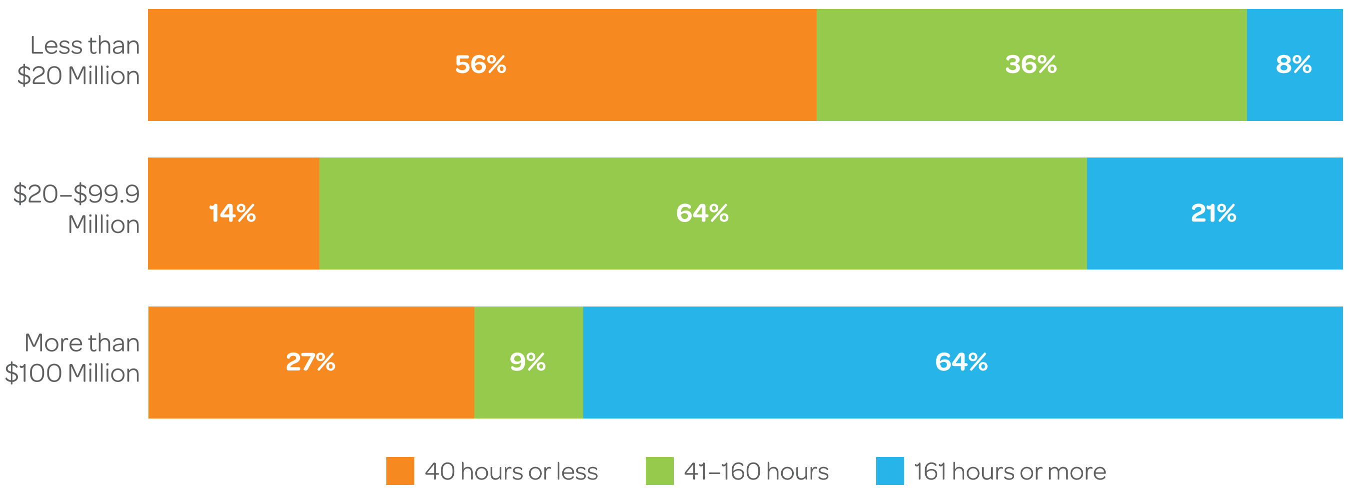
Cost of Compliance Forecast



Audit Volume



Hours Spent on Government Audits



CLARITY OUTLOOK

Finance and Financial Compliance

Recovery and a return to "more normal" operations will be the focus for small businesses in 2021. Along with a bounce back in revenues for these companies, profitability through efficiency and stability will be a major focus for all businesses.

The return from a year of disruption will entail a careful analysis of how to make the most of scarce resources using enhanced software tools, finding and retaining the best employees and a focus on diversification to broaden and reduce the risk in companies' revenue bases.

Attention to compliance requirements and audit preparations are expected to put companies on solid footing with regard to oversight. Understanding the process and requirements up front, and preparing accordingly, will allow companies to avoid unnecessary delays or potentially losing business.

SECTION THREE

Project and Risk Management

68%

Projects that were on or ahead of schedule fell to 68% overall from 78% the prior year.

While the pandemic may have contributed somewhat to this decline, the trend has been ongoing for years.

Headcounts in project and risk management were cut and KPI tracking was down in 2020, as companies focused on the top and bottom lines during the pandemic. This compromised performance, a trend that needs to be reversed in 2021 via getting initial project scope right and applying the right resources to meeting contract demands.

Last year, the Study reported that companies had trouble finding and training replacements as more experienced project managers began to retire. The expectation at the time was that companies would accelerate efforts to recruit talent and invest in better project management tools to increase efficiency.

With the arrival of the pandemic, companies instead reduced headcounts in support functions and focused resources toward business continuity. The effect was clear, as more projects fell behind schedule or came in over budget.

TOP THREE PROJECT AND RISK MANAGEMENT CHALLENGES

1 Alignment with executive management

2 Inexperienced project managers with insufficient software tools and inadequate, sidelined project management procedures

3 Project scoping

At the same time, change order wins decreased significantly, implying scoping problems.

Improved communications with other enterprise functions and better software tools to monitor and analyze project progress would flag problems earlier and facilitate reduced friction from costly changes that cannot be recaptured. It is essential that businesses invest in the best tools for risk and schedule management, while ensuring that employees know how to use them.

Now that businesses are emerging from the effects of the pandemic, companies should turn their attention to key functions that directly support project success and curtail risk.

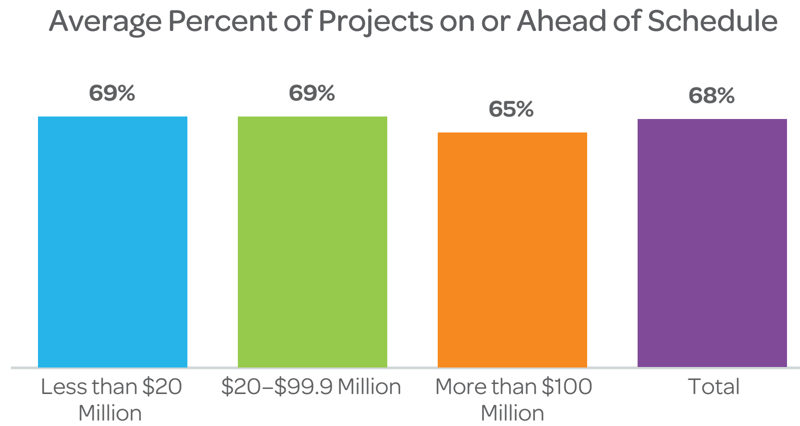
Beyond factors associated with the pandemic, businesses pointed to poor scoping as a real challenge.

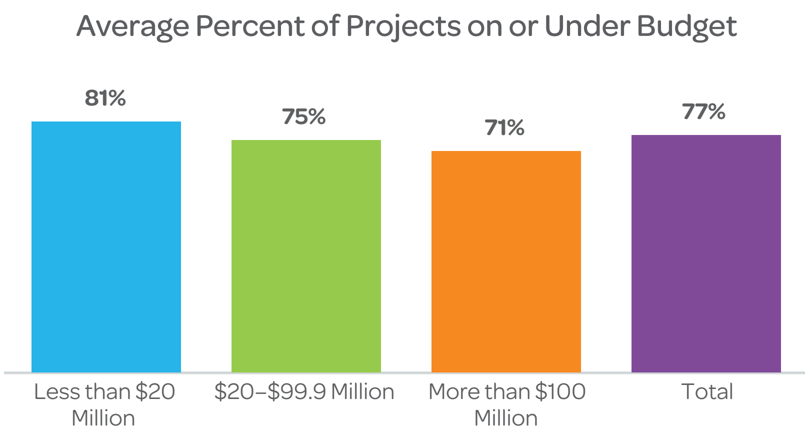
Project Performance

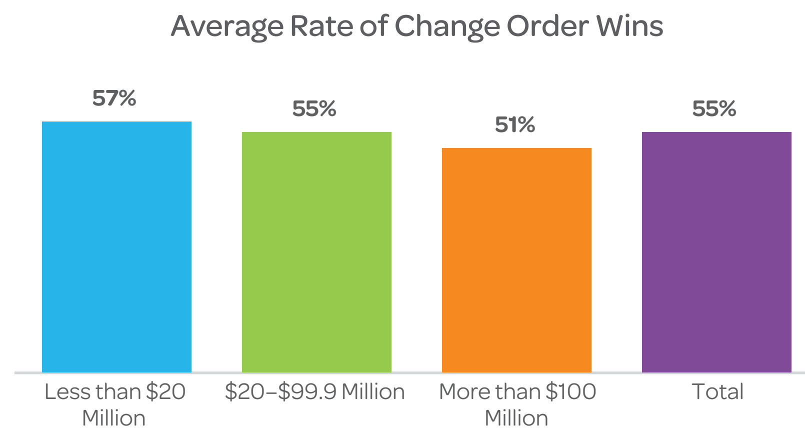
All sizes of businesses experienced a decrease in the percent of projects on or under budget. Small businesses saw a 5% reduction, while large companies experienced a 4% decline.

Similarly, more projects fell behind schedule. There was a 10 percentage point decline year over year, with small businesses falling by 15 percentage points. The effect of these shortfalls on project profitability, along with customer satisfaction, is substantial. If companies cannot reverse this trend, customer loyalty will be in jeopardy.

In 2020, businesses were less likely to win change orders, a notable problem for large businesses which experienced a 16% decline. Customers are growing less tolerant of change orders, pressuring businesses to improve project scoping and manage projects to contract specifications. As companies win larger, more complex projects with more subcontractors, risk increases.

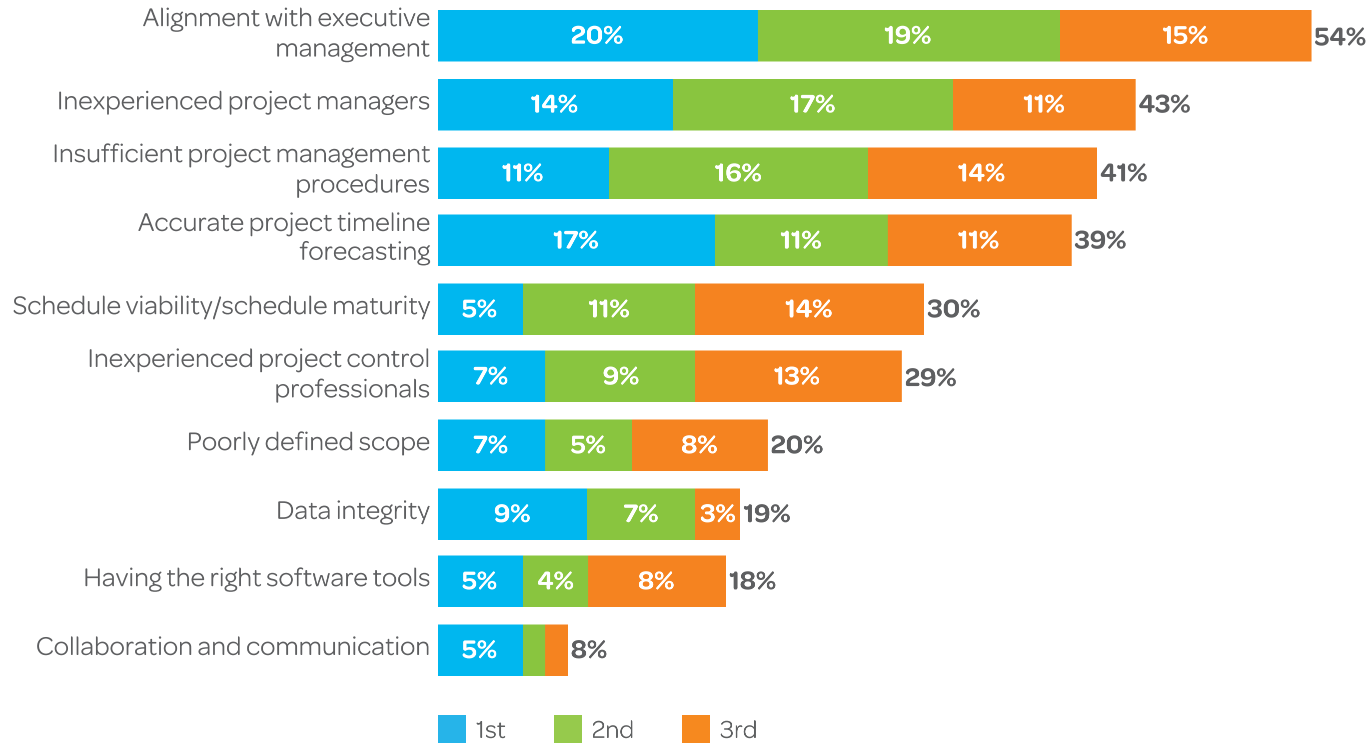






Top Project Management Challenges

Many of the challenges cited in 2020 were attributed to inexperience among project management professionals, insufficient processes and misalignment with executive management. This at least partially explains why companies felt challenged to produce accurate project timelines and budget forecasts.



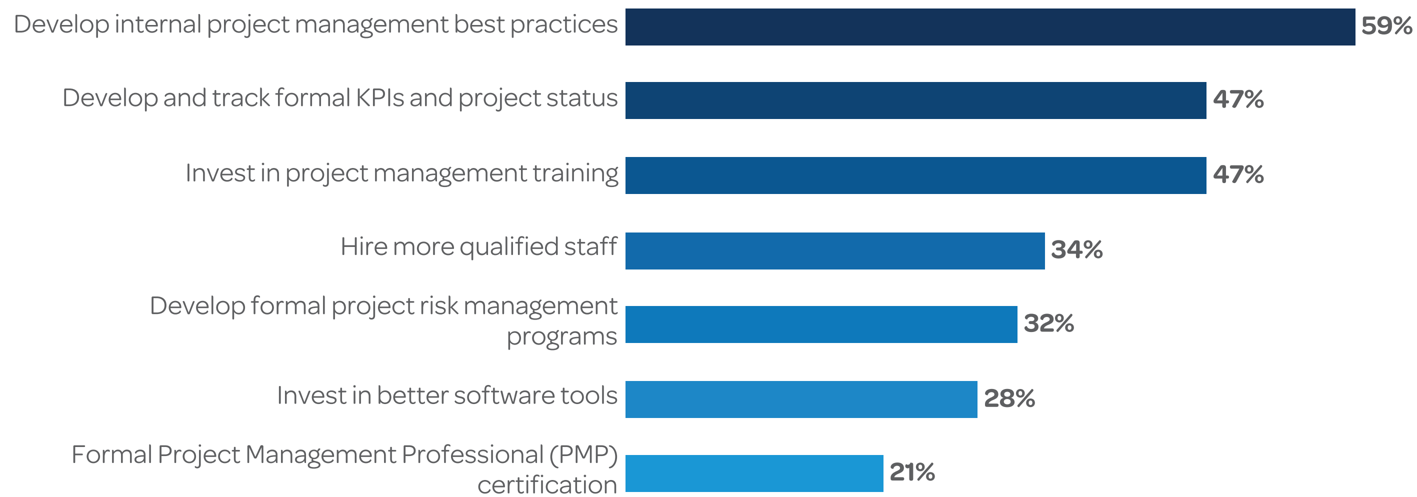
77%

Percent of projects on or under budget, down four percentage points.

Businesses of all sizes continue to struggle with accurately forecasting project scope.

Addressing Top Project Management Challenges

Many of the solutions to project management challenges revolve around hiring and training project management professionals. Developing best practices and investing in better software tools are foundational to raising the level of project management productivity. Project managers understand their value potential, indicating strong interest in identifying and tracking KPIs to better inform cross-functional teams throughout the project lifecycle.

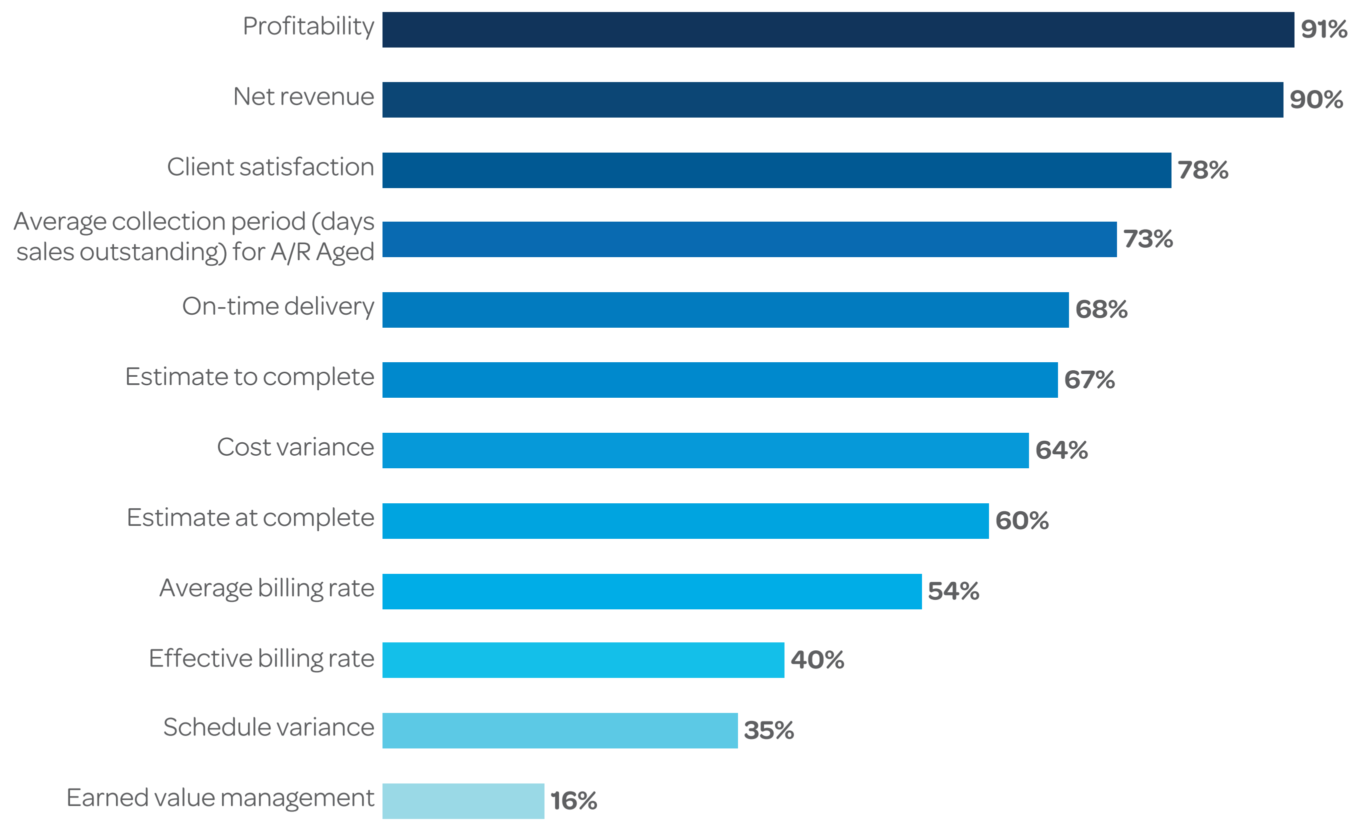


The Need for KPIs

The diminished headcount in project and risk management, along with less experienced project managers, compounded all challenges during the pandemic year. While nearly all respondents tracked profitability and net revenue, other important indicators received much less attention. Effective and average billing rates declined by more than 10 percentage points year over year.

Whether due to lack of visibility because of insufficient tools and integration or lower headcounts – or both – the data shows that less focus on KPIs results in poorer overall performance on key contract success factors.

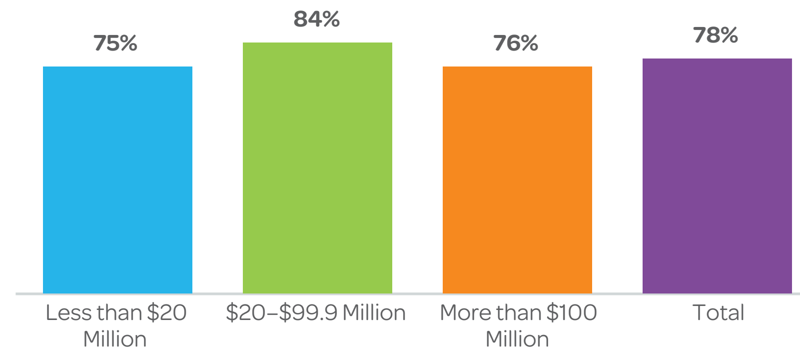
KPIs Currently Tracked



Forecasting

The ability to accurately forecast costs from start to finish on a project is key to profitability. In 2020, the accuracy for estimate at completion (EAC) and estimate to complete (ETC) forecasts slipped marginally, most notably among small businesses. As costs change constantly during a project, the importance of accurately forecasting how these changes will impact overall budget cannot be overstated. Managers must have the right software tools to track costs and integrate other functions and must know how to use them. performance on key contract success factors.

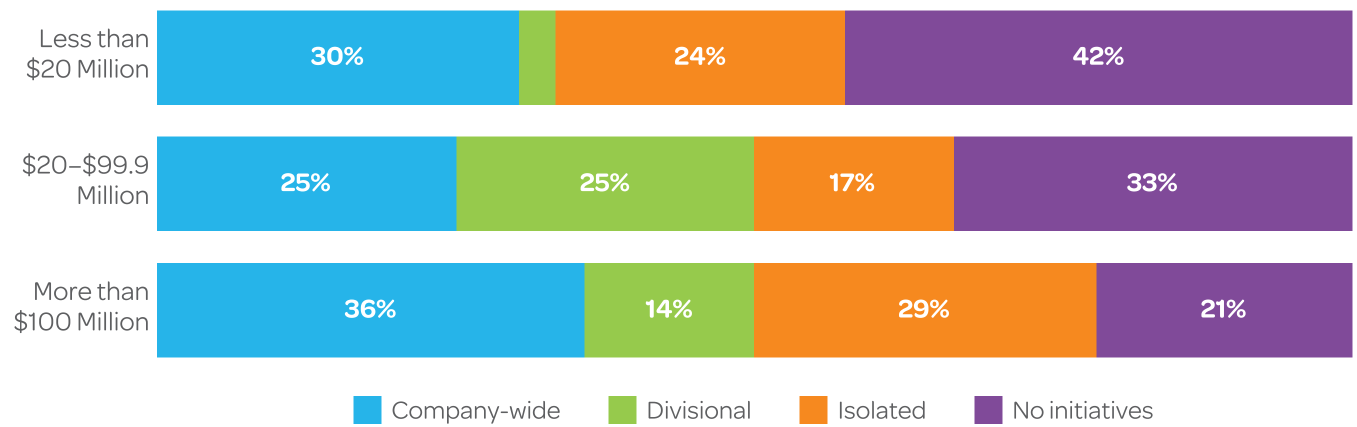
Average Accuracy of EAC and ETC Forecasts



Risk Assessment

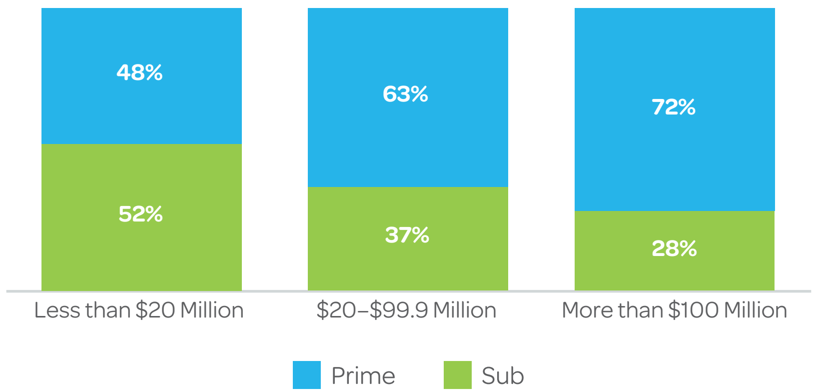
Fewer businesses in 2020 maintained company-wide risk and opportunity management. Forty-two percent (42%) of small businesses indicated they took no initiatives at all, while even large business lacked risk and opportunity management activity in 21% of cases.

Scope of Risk and Opportunity Management



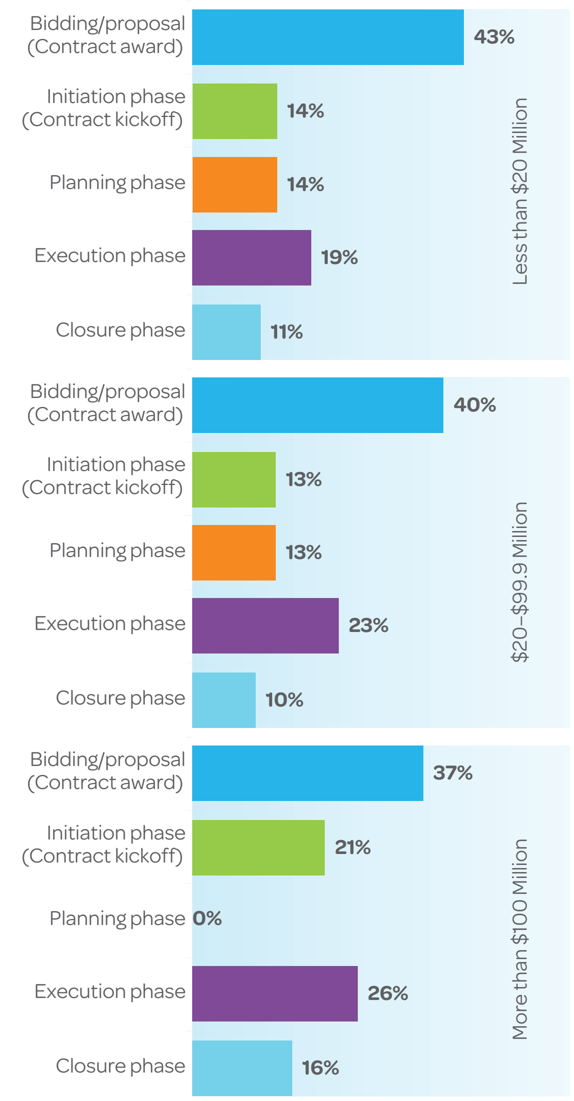
Primes versus Subcontracts

The risk management process is increasingly important in the face of rising subcontractor-to-prime ratios. Overall, 42% of contracts used subcontractors, an increase from 34% in 2019. As companies balance contract fulfillment and managing more outside resources over which they have limited control, implementing processes and tools to measure performance becomes more essential.



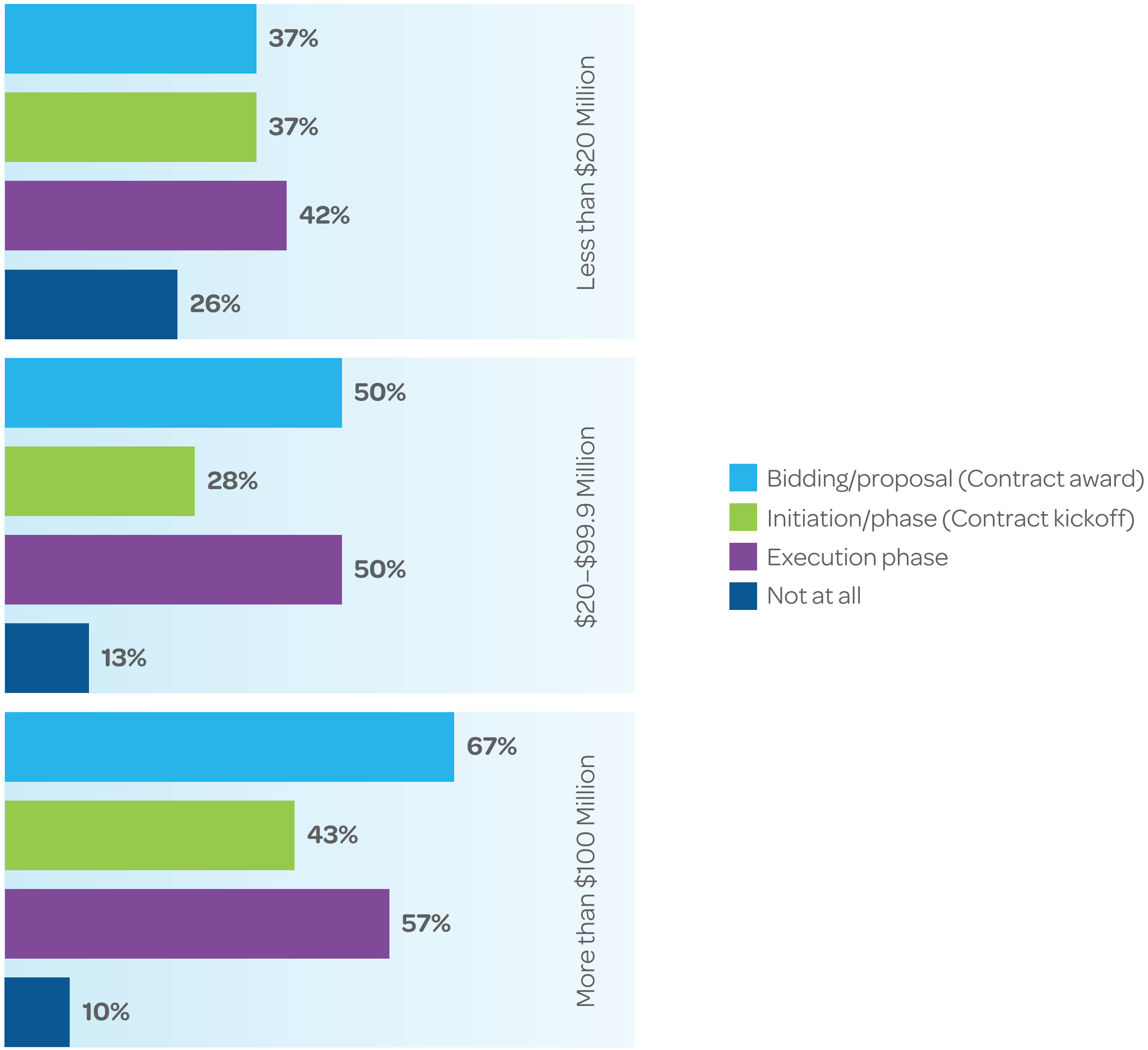
As projects become more complex, execution becomes a greater challenge. Along with managing more subcontrators with lower headcounts and inadequate tools, project managers cite poor scoping as factors that derail success.

Challenging Phase of Project Lifecycle to Execute



When Risk Analysis is Performed

Scheduling of risk analysis declined in fiscal year 2020, which is likely a reflection of lower headcount available to perform the function. It clearly is a contributor to the lower on-time and on-budget performance. If a problem is not seen and measured, it cannot be fixed.



CLARITY OUTLOOK

Project and Risk Management

Investment in adequate headcount, training and employee recruitment must gain more attention in 2021. As businesses return to normalized operations, reinstating project and risk management processes and tracking KPIs will reverse downward performance trends.

Most importantly, businesses need to recruit top project management professionals to replace retiring managers. Existing employees need the tools and training to do the job properly throughout the lifecycle of every project. The ability to accurately scope and track project progress through established best practices will improve time and budget performance.

Companies cannot afford to maintain reduced budgets and headcounts during a business rebound if they hope to avoid underperforming on contracts. If project risk is unchecked and KPIs that signal oncoming problems are ignored, businesses cannot expect to regain and grow profits and risk losing future opportunities. The declining performance in on-time and under-budget contracts clearly supports this.

SECTION FOUR

Human Capital Management

39%

Managing a distributed workforce is a top challenge.

The switch to a distributed workforce driven by the pandemic forced companies to operate in new ways, creating a need for greater collaboration and reliance on technology.

With anticipated revenue growth for 2021, the competition for talent is expected to increase. Employees that may have stayed in place in 2020 due to uncertainty in the market are anticipated to begin exploring new opportunities. Geographical expansion of the talent pool was accelerated by the pandemic and will likely remain a reality longer term, increasing access and competition for top talent. It also presents the possibility of changes to compensation systems. Companies may be able to adjust compensation for individuals working in areas with a lower cost of living.

While businesses continue to look to rebranding to become more attractive to top talent and younger workers, the benefit of remote and more flexible work options will provide additional appeal. Employees who have been successfully working remotely will be reluctant to give up that benefit, so companies that insist upon a full return to the office will potentially decrease in competitive appeal.

TOP THREE HUMAN CAPITAL MANAGEMENT CHALLENGES

1 Attracting and retaining top qualified talent

2 Succession and career development planning

3 Managing a distributed workforce

The advent of this remote or blended workforce gave rise to new management needs and support requirements. Creating a virtual workplace and fostering client collaboration was a top technology trend. It also created the need for a greater focus on cybersecurity to ensure that remote workers were not compromising security and putting engagements at risk. Companies seeking best-in-class methods for workforce management will need technology to further facilitate success.

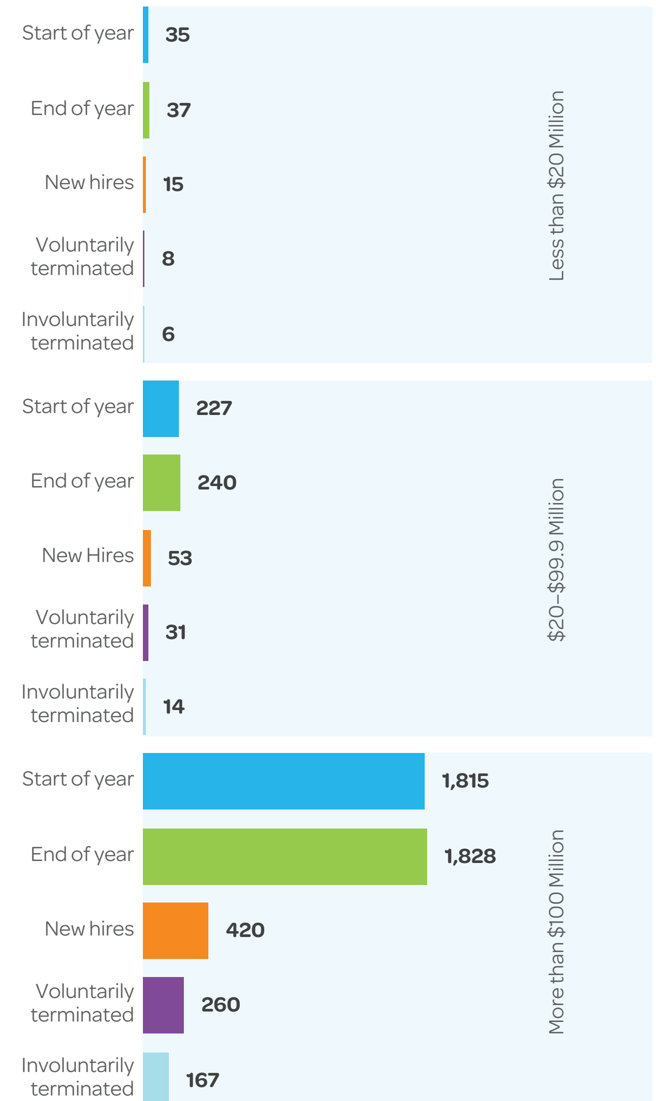
Remote work is here to stay and offers new competitive advantages.

Trends in Employment and Turnover

Despite the changes presented by the pandemic, namely a focus on business continuity and greater recruiting and retention challenges, businesses of all sizes increased headcount. Despite that, regrettable attrition – losing employees that companies would rather retain – rose, with 67% of businesses reporting an increase. This is a troubling trend that will continue if companies do not take the time to assess why top talent is choosing to exit.

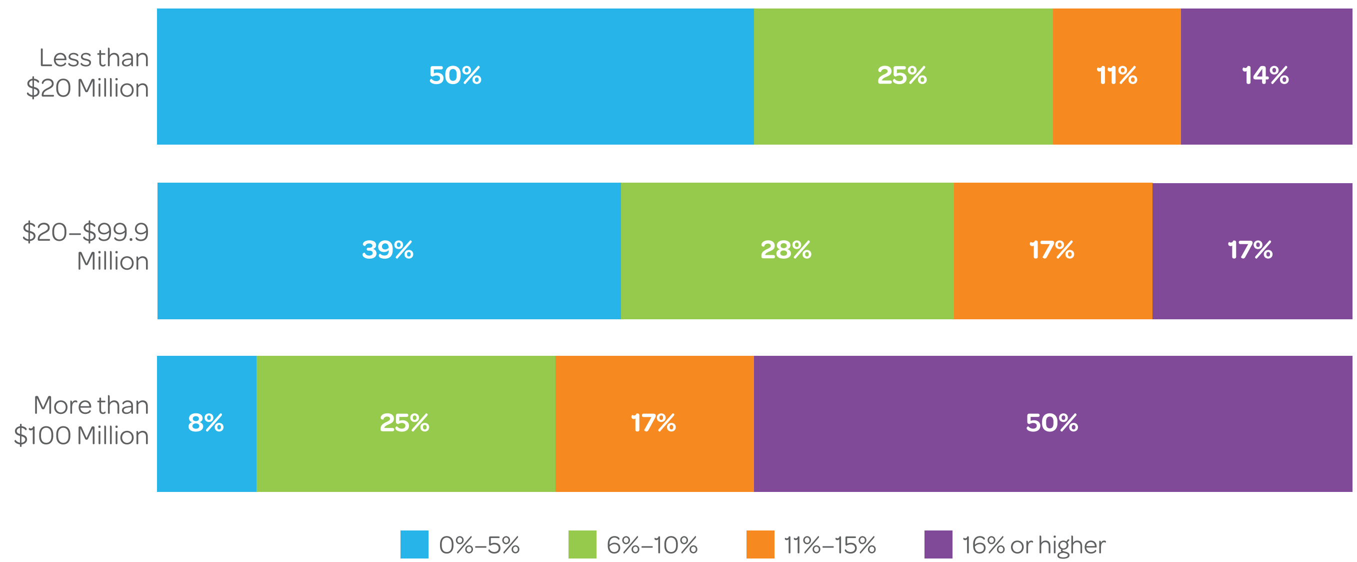
The Society for Human Resources Management (SHRM) regards 3% involuntary terminations as a best-in-class target. Government contracting companies are operating at considerably higher rates. This raises the question as to whether hiring processes were weak or the need to reduce headcounts affected the totals.

Average Firm Headcount in 2020



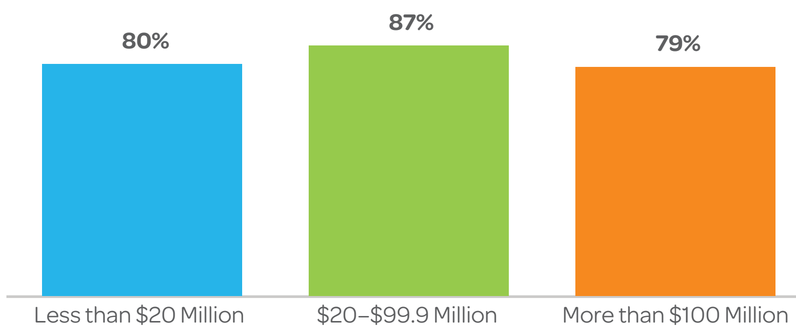
Primes versus Subcontracts

The composite turnover rate for full-time employees (FTEs) declined but remained high with 22% overall reporting 16% or higher turnover. Large businesses were affected the most.



Retention Rate

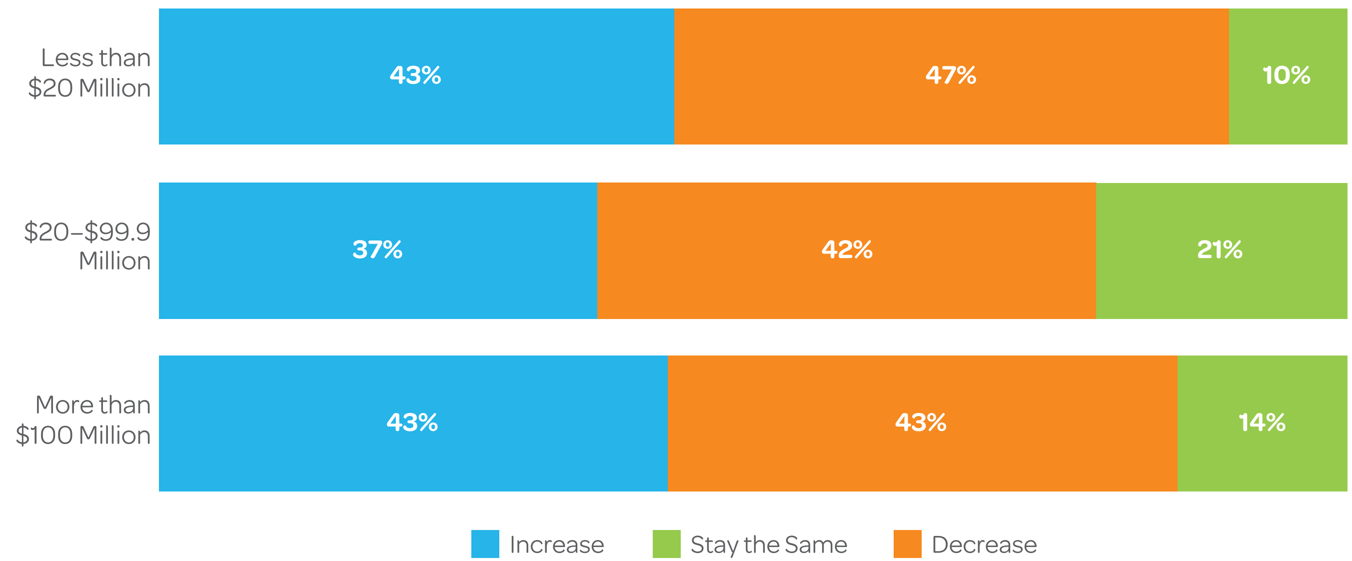
The retention rate increased slightly in 2020 to 82%. Medium-sized businesses experienced an increase of 10 percentage points, while other sizes of companies remained relatively flat.



Change in Open Positions

Consistent with a lower turnover rate, fewer respondents to the Study indicated an increase in open positions year over year. Most indicated no change or slight growth in the number, representing a decrease in open positions relative to 2019.

The average time needed to fill open positions has expanded slightly, as more businesses indicated a shift from zero to 30 days to 31 to 60 days over the past year. The difficulties of recruiting and onboarding during the pandemic may have been a factor in this change.



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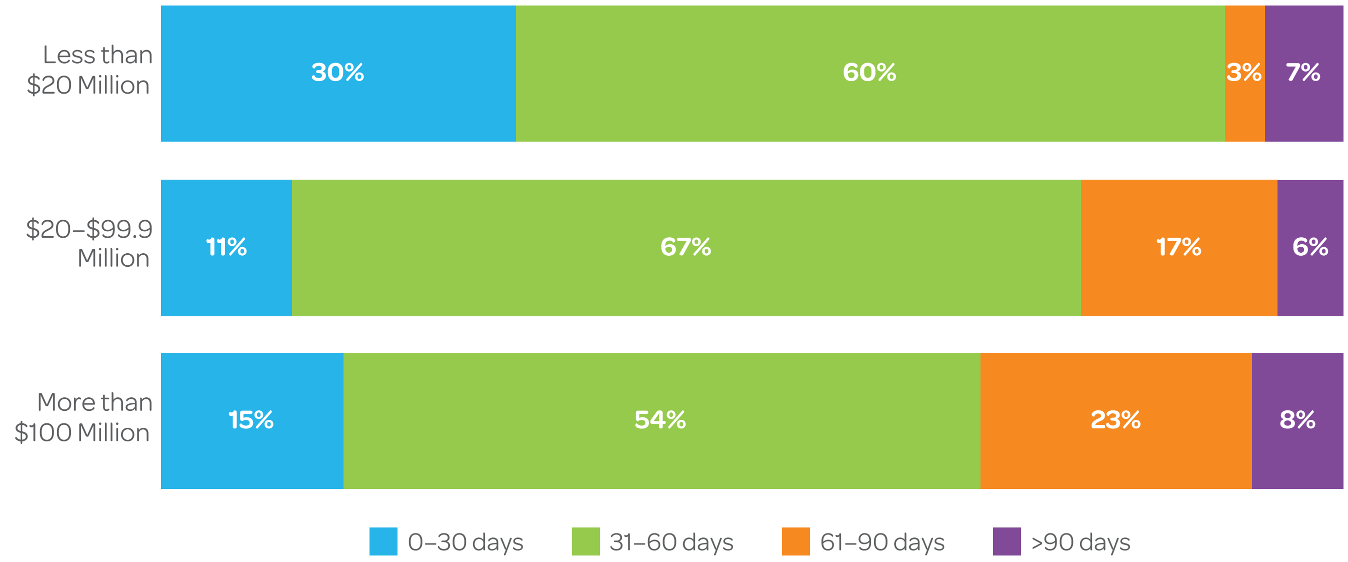
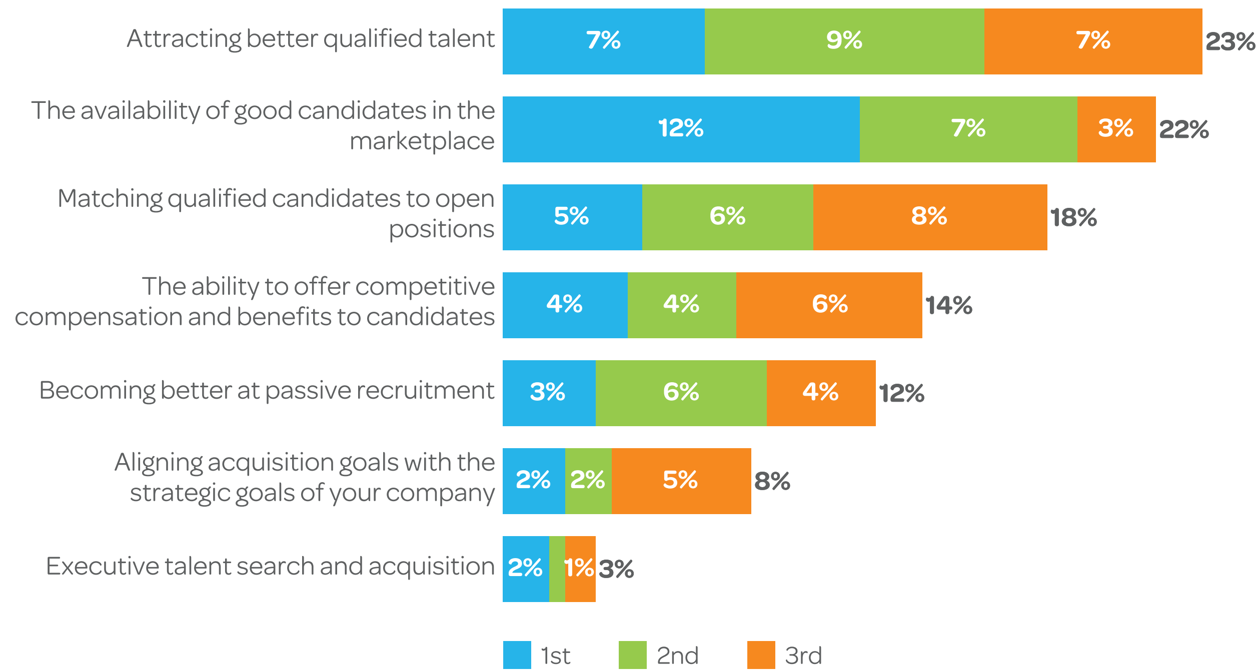


Top Talent Acquisition Challenges

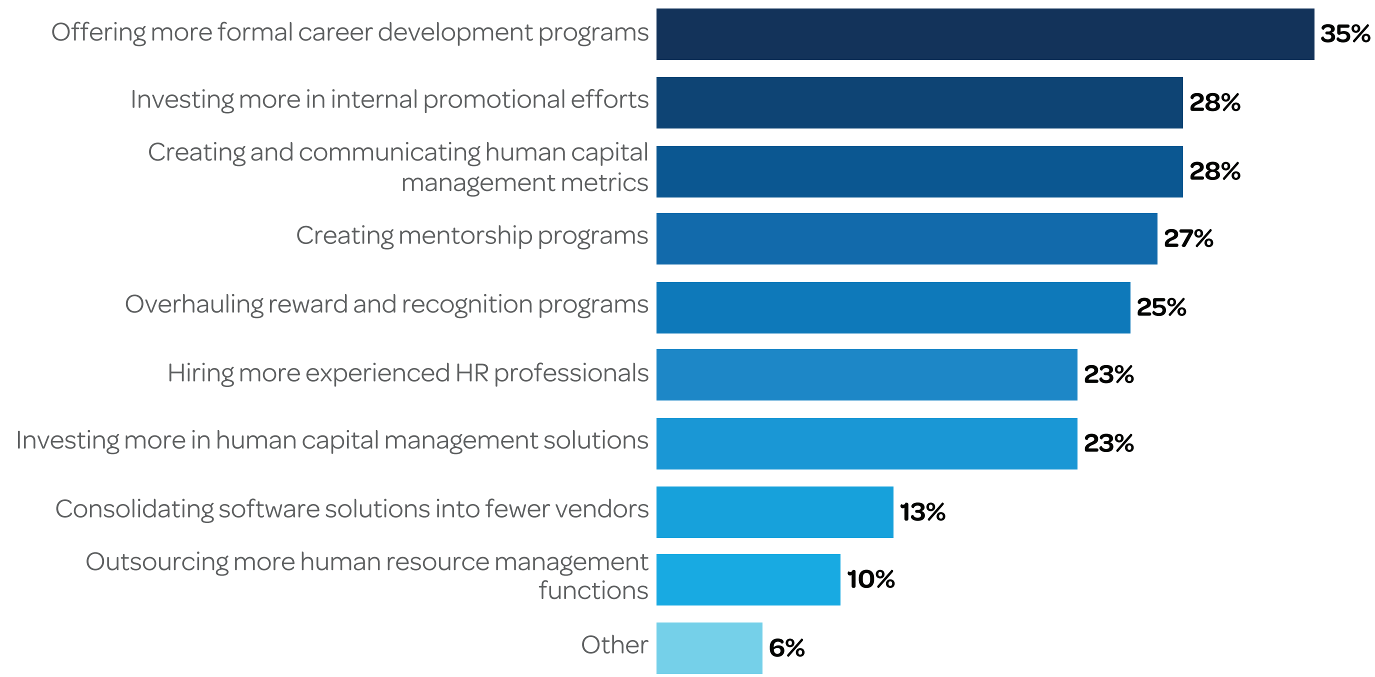
The competition for top talent remains a major challenge and concern, along with the availability of good candidates in the marketplace. Twenty-three percent (23%) of respondents rated attracting better quality talent as their top concern, a five percentage-point increase year over year. The availability of good candidates in the marketplace fell to second place versus a year ago. The ability of companies to cast a wider net due to remote working may have affected this.



Addressing Top Talent Acquisition Challenges

For several years, respondents to the Study have cited rebranding as a method of reaching better qualified talent. It jumped to first place in 2020, with outsourcing recruitment more and increasing incentive for employee referrals dropping to second and third place respectively. Rebranding can be difficult to accomplish without changing underlying practices and policies, particularly in the face of more flexible approaches among competitors. The continued adoption of remote work and flexible hours could serve to attract a broader and younger talent pool and be a step toward winning over the competition for talent.

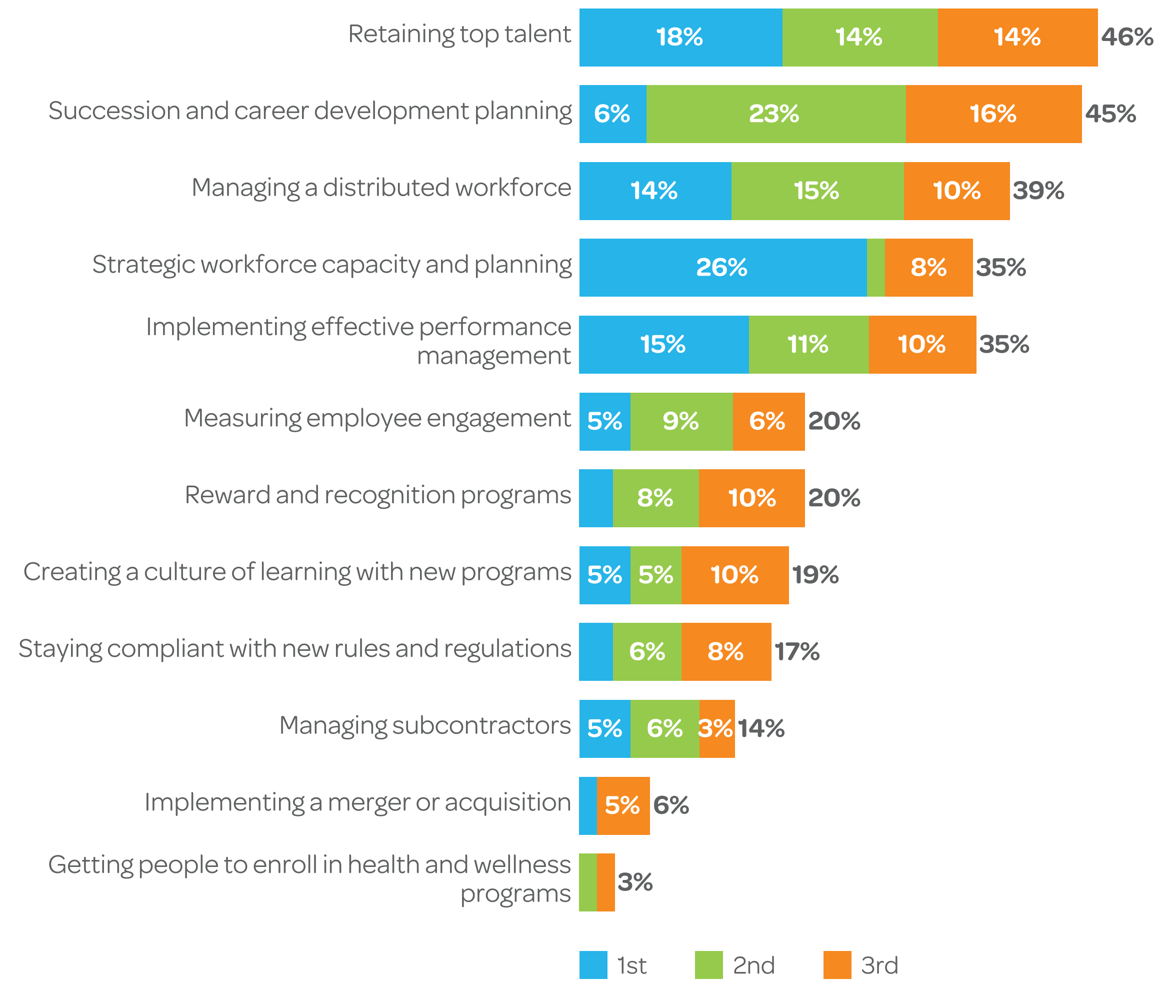
Hiring more recruiters and switching to a new talent acquisition software solution dropped in importance as more companies made do with existing resources, but may have a longer-term negative impact on talent management overall as investment in this area lags behind.



Top Human Capital Management Challenges

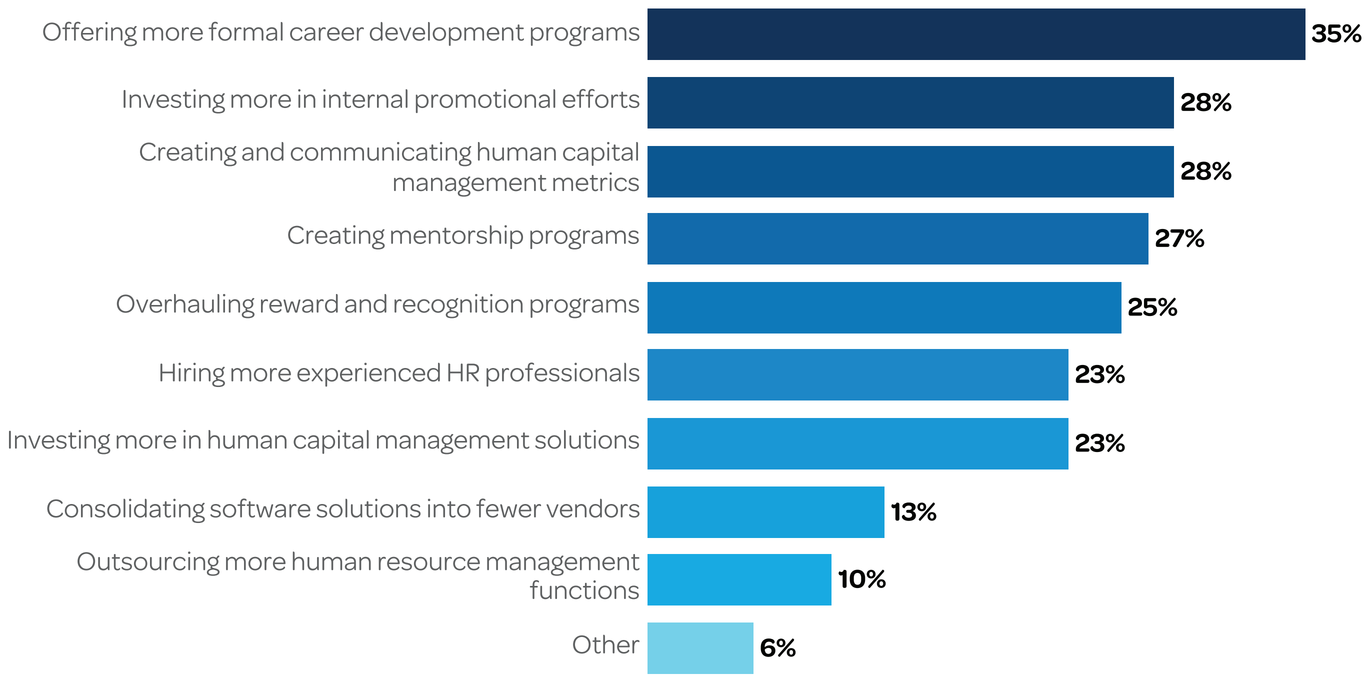
With the changes brought about by the pandemic, managing a distributed workforce became a focus of importance for the first time. Thirty-nine percent (39%) of respondents rated this as one of their top three challenges.

While retaining top talent remained a key focus, it dropped in importance year over year, with strategic workforce capacity and planning rising as the first choice. With the growing need to accommodate a blended or fully virtual workforce, companies had to quickly adapt with new ways of managing teams and project delivery. As the pandemic recedes, companies must strike a new balance with workforce policies and evaluate which ways of work to return to and which to adopt permanently.



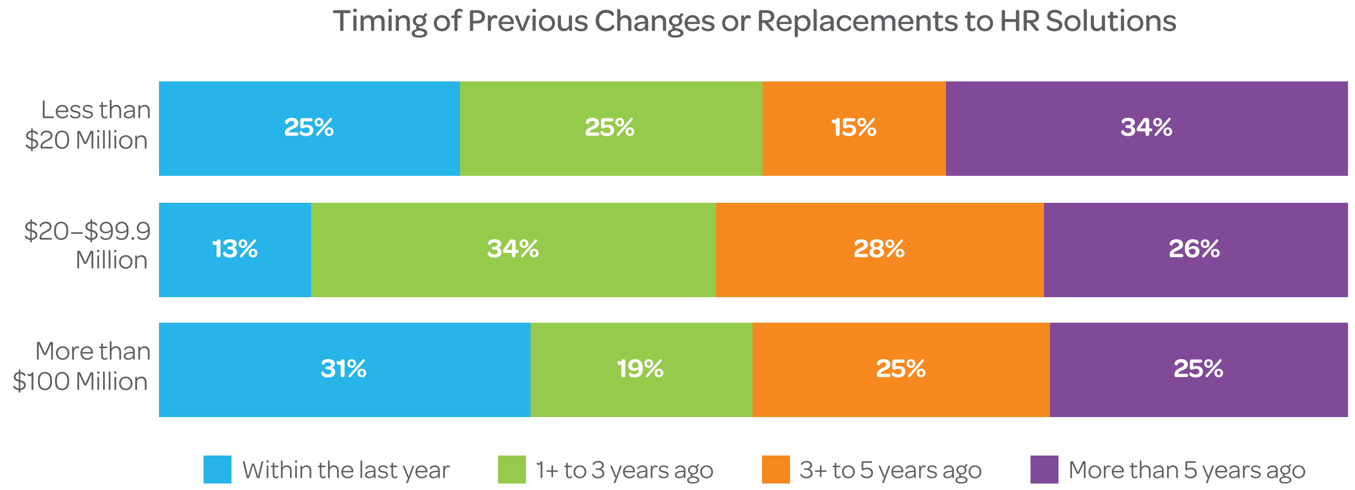
Addressing Top Human Capital Management Challenges

Businesses are seeking to retain top talent by offering more formal career development programs and investing in more internal promotional efforts. Twenty-eight percent (28%) of respondents indicated an interest in creating and communicating human capital metrics, a slight decrease from the prior year. With the need to reassess workplace policies and remote work, investing more in human capital management solutions would provide added tools and insights to aid in key decision making. Only 23% of respondents cited this as a priority, down seven points year over year, implying that companies held back on investing in new tools in 2020.



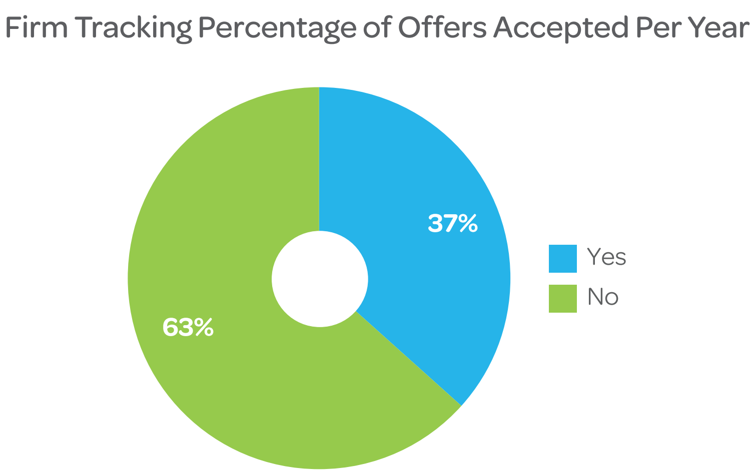
Timing of Updates to Human Capital Management Solutions

Fifty percent (50%) of companies have significantly added to or replaced their human capital management solutions within the past three years. Small businesses reported that 34% of solutions were more than five years old. Twenty-nine percent (29%) of companies overall had not added to or replaced their human capital management solutions in over five years.



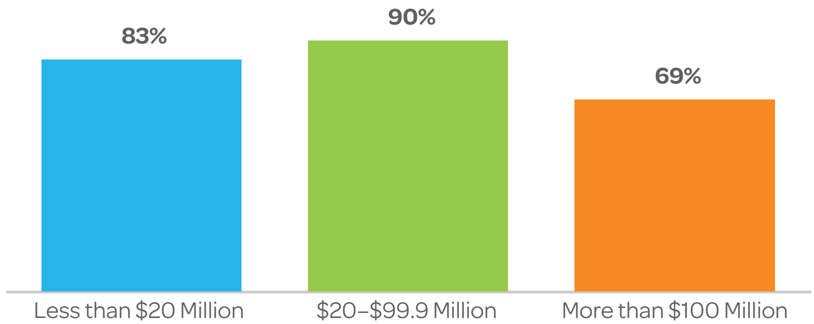
Hiring in 2020

Fully 63% of Study respondents indicated that they do not track the percentage of offers accepted on an annual basis. This may indicate that an opportunity to understand why offers are rejected is being missed. This could also help shed light on the reason for the higher-than-average regrettable attrition also reported in the study this year.



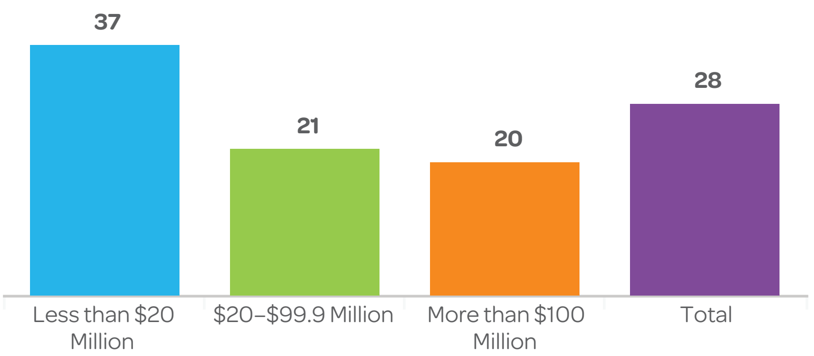
Average Offers Accepted

The average number of offers accepted in 2020 increased slightly. Both small and medium-sized businesses showed upticks in the average percentage of accepted offers. The exception was large businesses, which saw acceptances fall from 76% in 2019 to 69% in 2020. Employee referrals continued to be an important source of new hires, as this metric increased overall from 22 to 25 in 2020. Each business size indicated improvements from the previous year.



Average New-Hire-to-Bill Time

The time that it takes for a new hire to be financially productive by billing expanded in 2020. Medium-sized businesses reported an increase in the average number of days for new hires to be billable, while large businesses saw a decline in the time required during the same period. This could indicate a need for revamped onboarding practices to facilitate remote workers unable to attend in-person training in the earliest days of their employment.



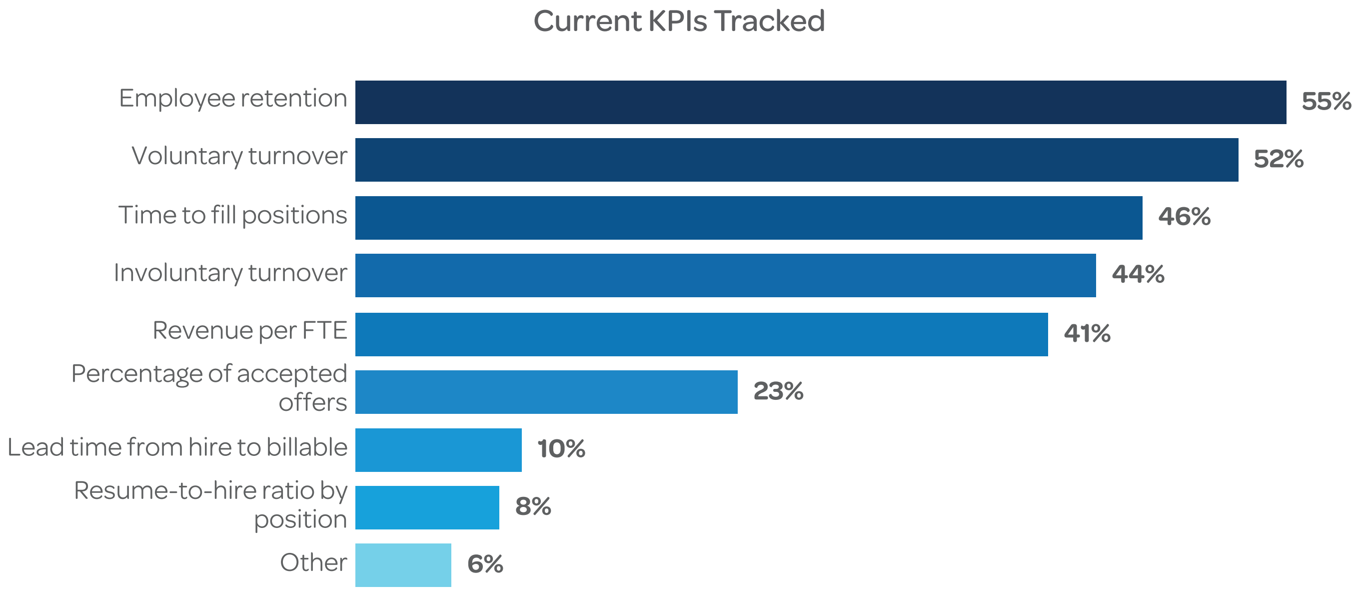
61%

Virtual workplace and collaboration surged in importance as a technology trend.

While a remote or even blended workforce presents challenges, it also surfaces opportunities for attracting and retaining talent.

Tracking Human Capital Management Metrics

Companies worked to analyze human capital management metrics through a number of KPIs. The top three tracked continue to focus on sourcing and retaining talent, voluntary turnover and the time to fill positions. These metrics received somewhat less concentration in 2020, however, with a notable increase in respondents citing revenue per full-time employee. That statistic rose in 2020 to 41% from 31% the previous year.

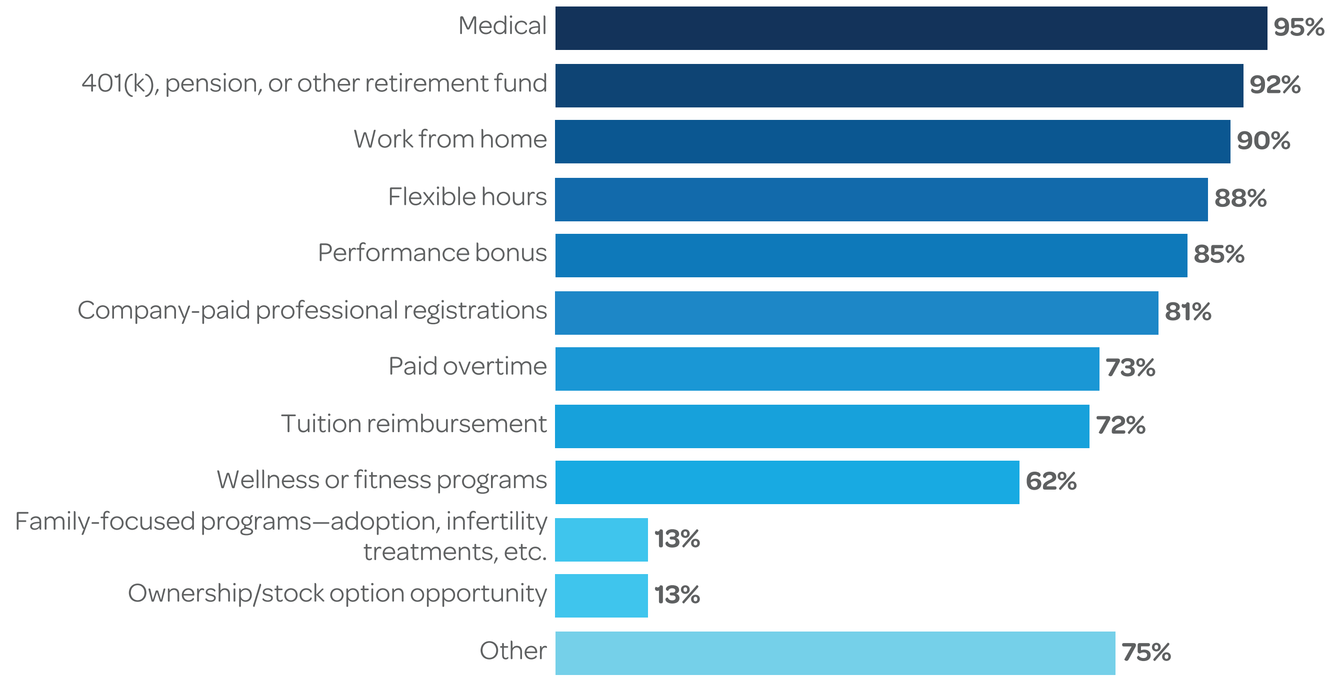


Benefits

Work from home and flexible hours increased dramatically in 2020 as the response to the pandemic necessitated these changes. These were the most-leveraged employee benefits, along with medical plans, 401(k)s and performance bonuses. Tuition reimbursement remained popular at 72% among Survey respondents.

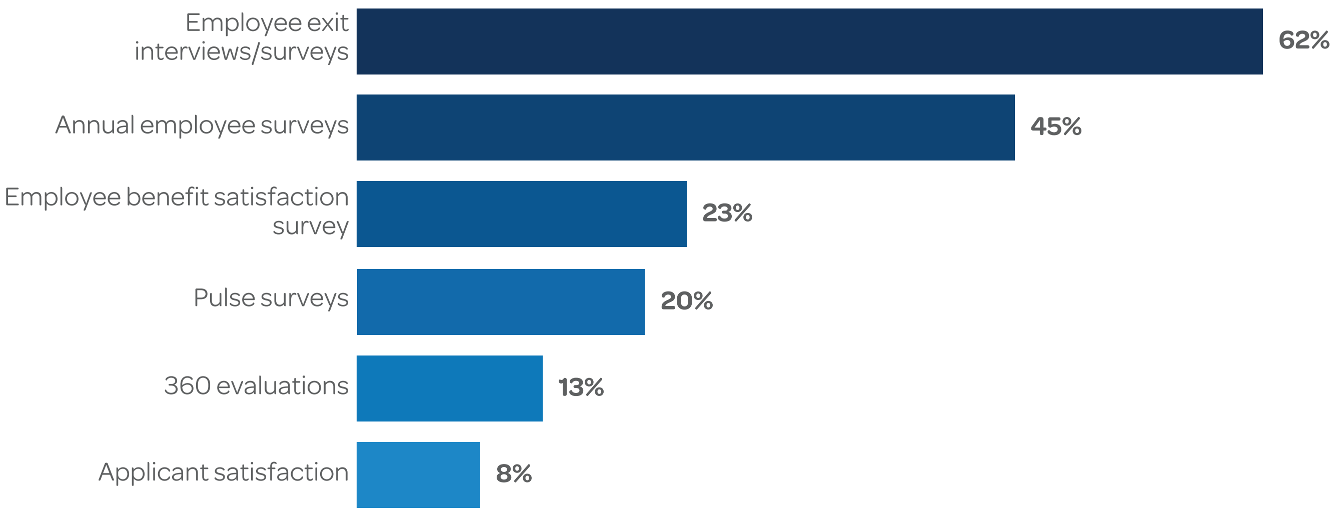
As the effects of the pandemic recede, it is likely that work from home and flexible hours will continue to be an important and popular benefit.

Employee Benefits Offered



Employee Engagement Surveys

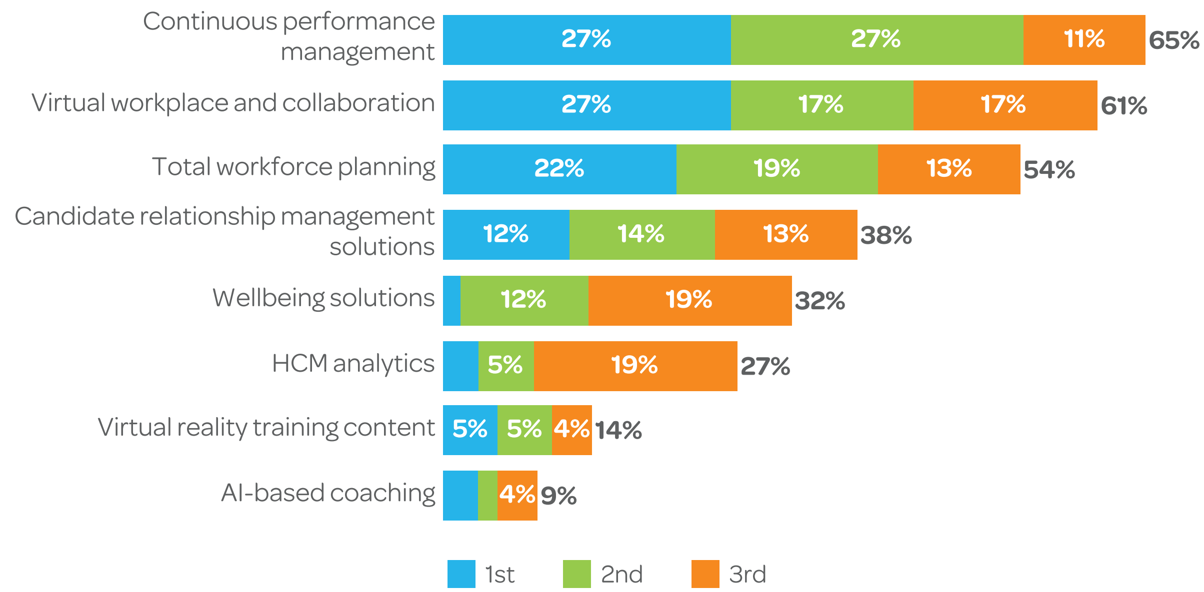
Annual employee surveys continue to be a leading method of measuring employee satisfaction, but saw a year-over-year decline, dropping five percentage point to 45% of respondents conducting them. Pulse surveys, shorter and more timely than annual surveys, increased year over year from 14% to 20%. Employee exit interviews and surveys were the top engagement survey method, with 62% of respondents naming it as the top choice among methods.



Technology Trends

The most important technology trend continues to be continuous performance management, followed closely by virtual workplace and collaboration, which surged in importance as business continuity challenges took center stage in 2020. Total workforce planning remained in third place as companies were challenged in managing a distributed workforce and effectively planning resourcing on projects while adapting to shut downs/slowdowns and shifting timelines.

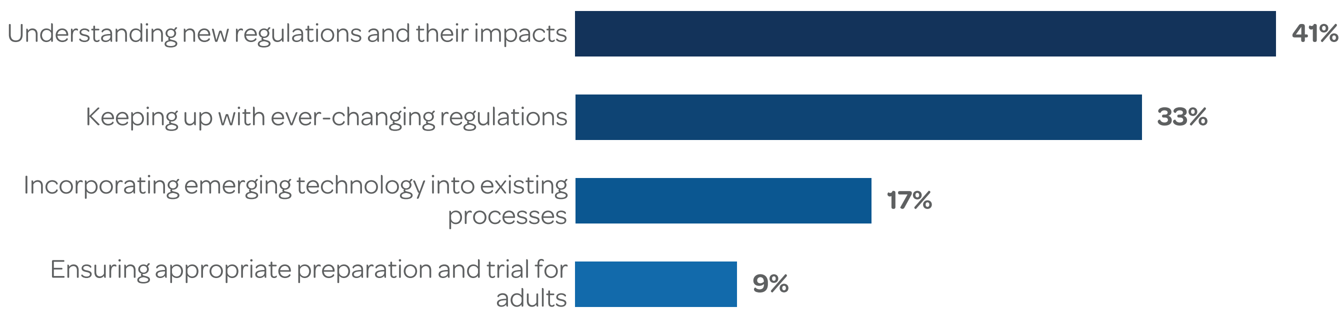
Technology Trends in Human Capital Management



Compliance

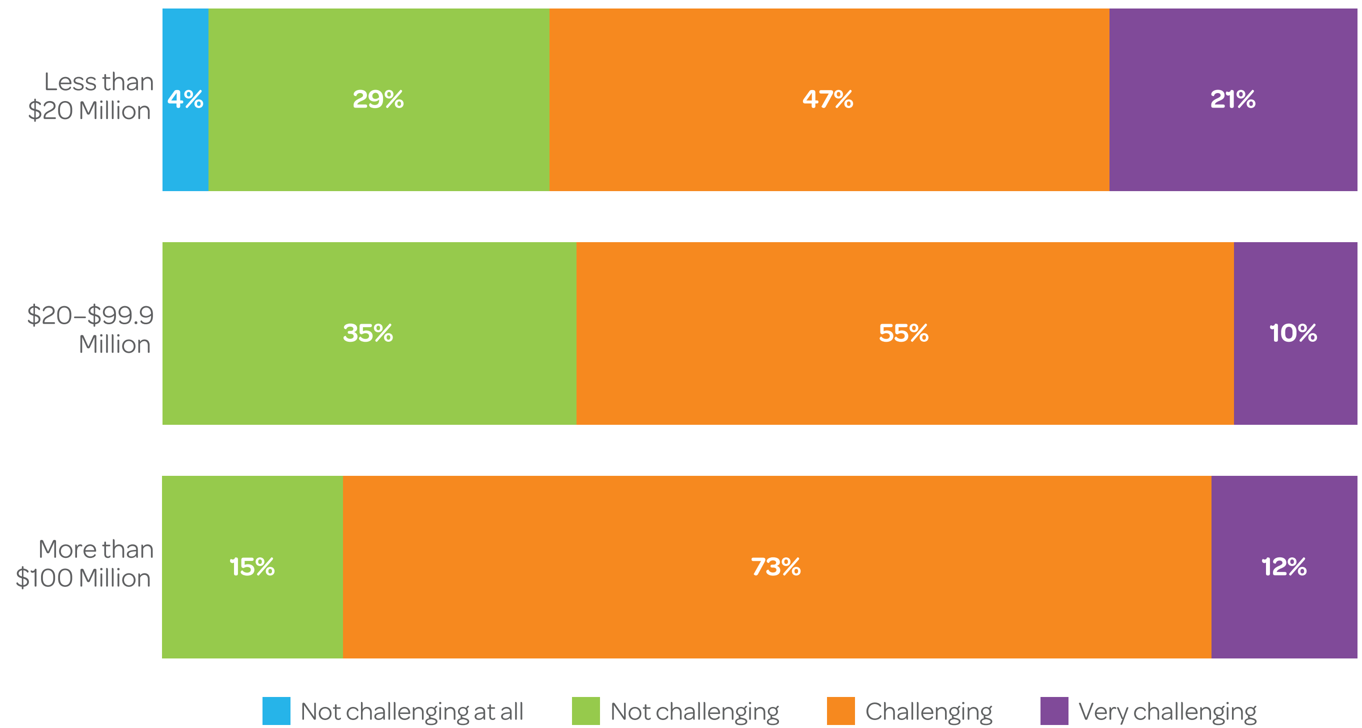
The greatest concern cited by respondents about human capital compliance continued to be understanding new regulations and their impacts. Keeping up with ever-changing regulations was still a top concern but dropped in significance. There was a notable bump this year with incorporating emerging technology into existing processes growing to 17% from 11% a year ago

Greatest Concern About Human Resources Compliance



Staying on Top of Changing HR Compliance Issues

Companies continue to consider it challenging to stay current with human capital compliance issues, which change frequently. Seventy-three percent (73%) of businesses report that staying on top of compliance issues is either challenging or very challenging. Eighty-six percent (86%) of large businesses also find it difficult. In addition, some pandemic-related funds also came with somewhat vague guidelines around retaining subcontractors that could also be contributing to these findings.



CLARITY OUTLOOK

Human Capital Management

The ongoing challenge to recruit the best and brightest workforce depends upon the available talent pool, as well as the attractiveness of the workplace. The emergence of a virtual workplace presented challenges, but it also surfaced opportunities in these areas to better attract and retain talent.

With the accelerated shift to a more remote or blended workforce, companies are no longer restricted to talent in a certain location for some roles, broadening the field of prospective hires. The benefits of remote work and flexible hours make companies more attractive to a younger, more tech-savvy pool of candidates. Government contracting firms would be wise to consider how to continue to leverage these practices moving forward.

Companies that leverage best-in-class methods for workforce management, including technology, will achieve higher rates of success in recruiting, retention and compliance. The sophistication of tools needs attention as the workforce morphs from in-office to remote and flexible working.

SECTION FIVE

Contract Management and Procurement

50%

In the face of increasing complexity, large business slashed contract management full-time employee headcount by more than 50%, while small and medium-sized businesses held on to exceedingly small staffs.

Companies did not leverage other resources or tools, like tracking software, to help compensate for headcount reduction.

Businesses were even more challenged in 2020 by reduced headcounts, which forced them to focus directly on top-priority KPIs and metrics such as profitability, net revenue and client satisfaction. Other metrics such as earned value management and measurement of billing rates were moved to the back burner.

Contract management and procurement teams are contributing to business success more strategically as more cloud-based solutions have come online, but there still is a long way to go. With continued migration to the cloud, businesses are leveraging multiple solutions through integration and providing views into a broader, more cross-functional set of KPIs, such as finance, human capital management, customer relationship management (CRM) and contract management. While progress is apparent, integration remains the biggest challenge, with financial integration in the crosshairs.

TOP THREE CONTRACT AND PROCUREMENT CHALLENGES

1. The need to integrate financial aspects of projects into project management tools and KPIs
2. Inexperienced project management professionals requiring greater professional development and access to more sophisticated tools
3. The continued need to integrate and leverage software solutions

Headcounts are at a bare minimum, with many full-time employees doing double duty running both contract management and procurement. Remaining employees are stretched and dialing back on lower priority or less accessible metrics.

Reliance on generic software and shared drives has increased despite the risks to security and efficiency. Basic features require extensive manual labor to create and maintain company-specific input, limiting the quality of information available. The ability to maintain data integrity is somewhat compromised, and time spent entering and tracking contract information into basic systems places further pressure on employees.

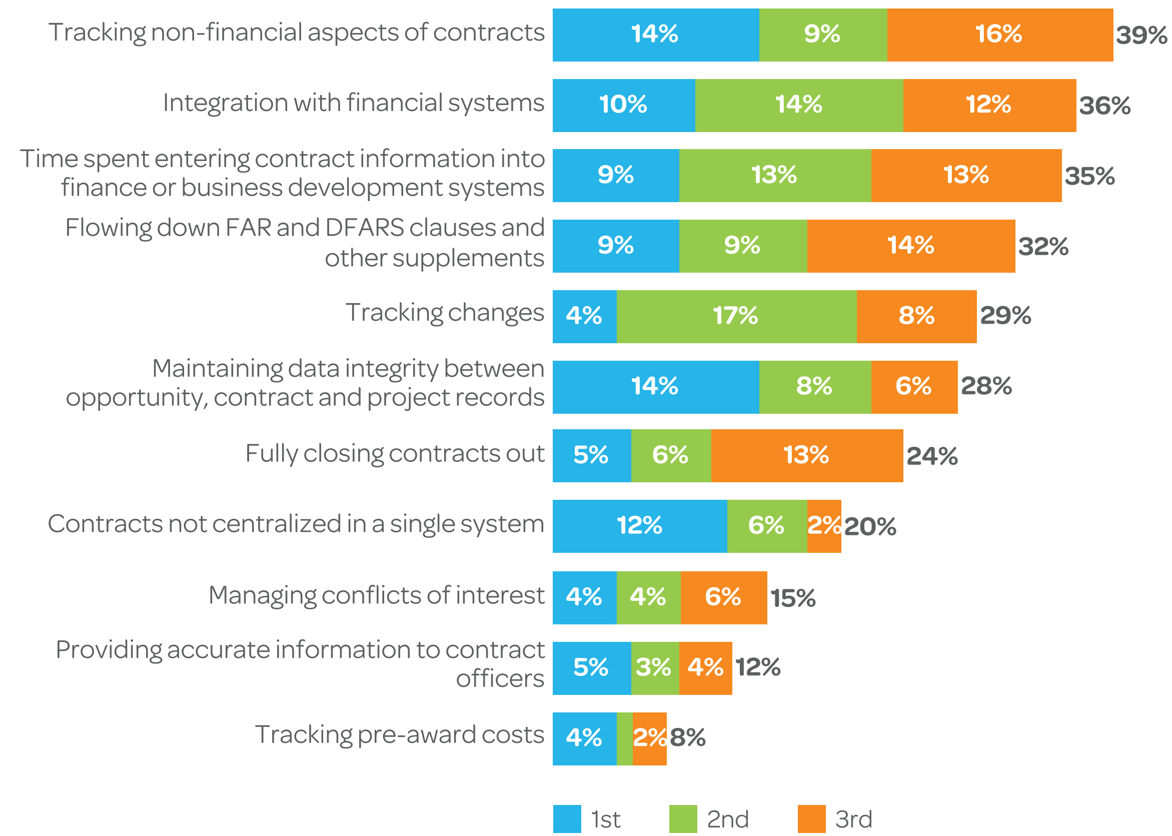
As in the past, attention to procurement is primarily devoted to two KPIs: direct versus indirect spend and days payable outstanding. Other factors, such as measuring procurement cycle time and dedicated full-time employees, received less attention in the pandemic year.

Financial metrics, like total savings achieved, purchase order (PO) status by supplier and spend by supplier, remained relatively stable.

Companies need to invest in people and leverage more robust tools to stay ahead of the growing complexity of projects and adequately advise executive teams.

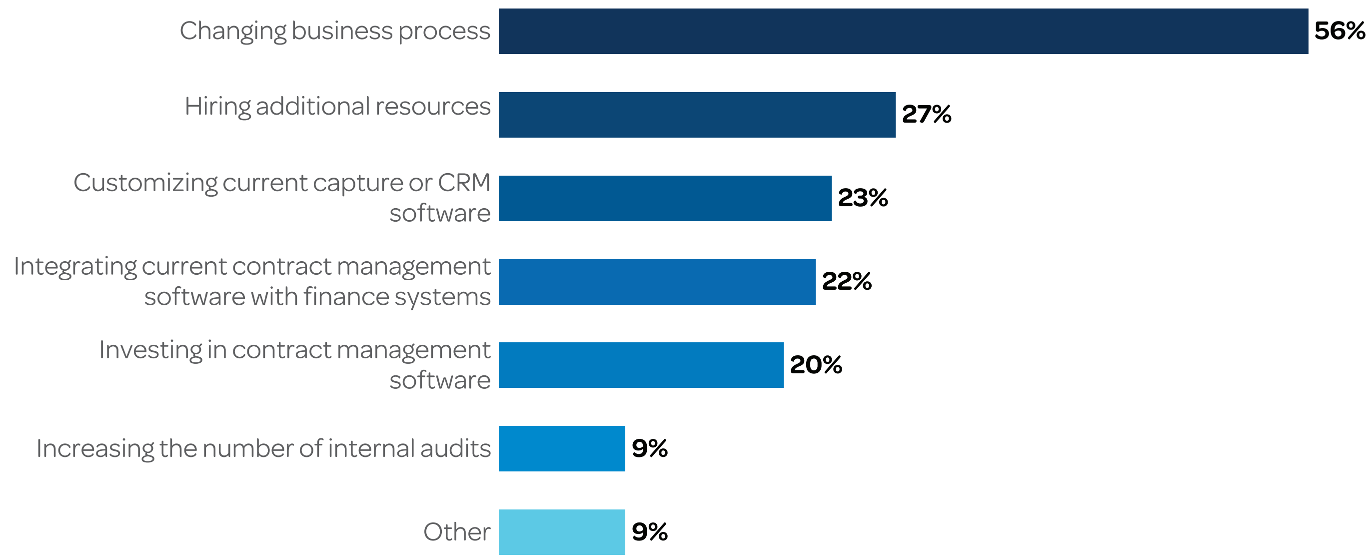
Top Contract Management Challenges

Contract management professionals recognize the potential impact that their function has on the enterprise's success. The ability for project teams to achieve contract objectives depends greatly on the integration of financials, project management and CRM/sales intelligence. Without a comprehensive, integrated perspective of these functions in the project management process, professionals in this area are hampered and will have trouble communicating effectively with others in the organization. As fully 20% of respondents do not have contracts centralized in a single system, there is much work to do.



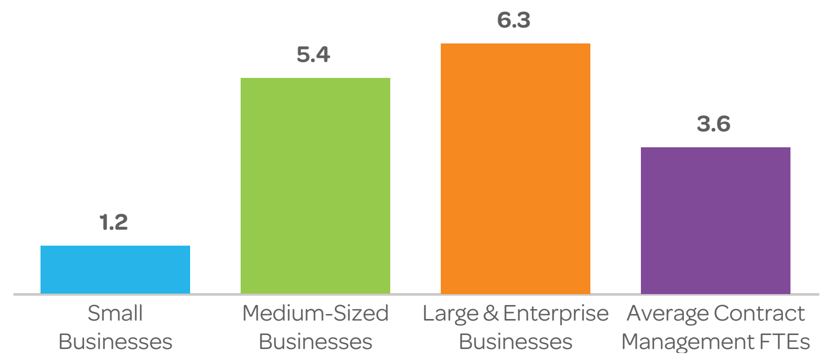
Addressing Top Contract Management Challenges

Businesses are dialing up the focus on changing business processes to address challenges; 56% of respondents cite this approach compared with 45% last year. This year's Study indicated that 27% would hire additional resources, while approximately one-quarter of respondents plan to customize and integrate their software. As businesses move and integrate more applications to the cloud, processes will improve and KPIs will become more accessible. Armed with business intelligence, contact management teams will contribute significantly to enterprise agility.



Full-Time Headcount in Contract Management

Small and medium-sized businesses retained their extremely small base of full-time contract management employees in 2020, while large companies cut headcount significantly. Headcount is at exceptionally low levels and actually shrank overall from 5.0 to 3.5 average full-time employees year over year. Reversal of this trend in 2021 as business returns to greater normality is imperative so that the workload is appropriately balanced.



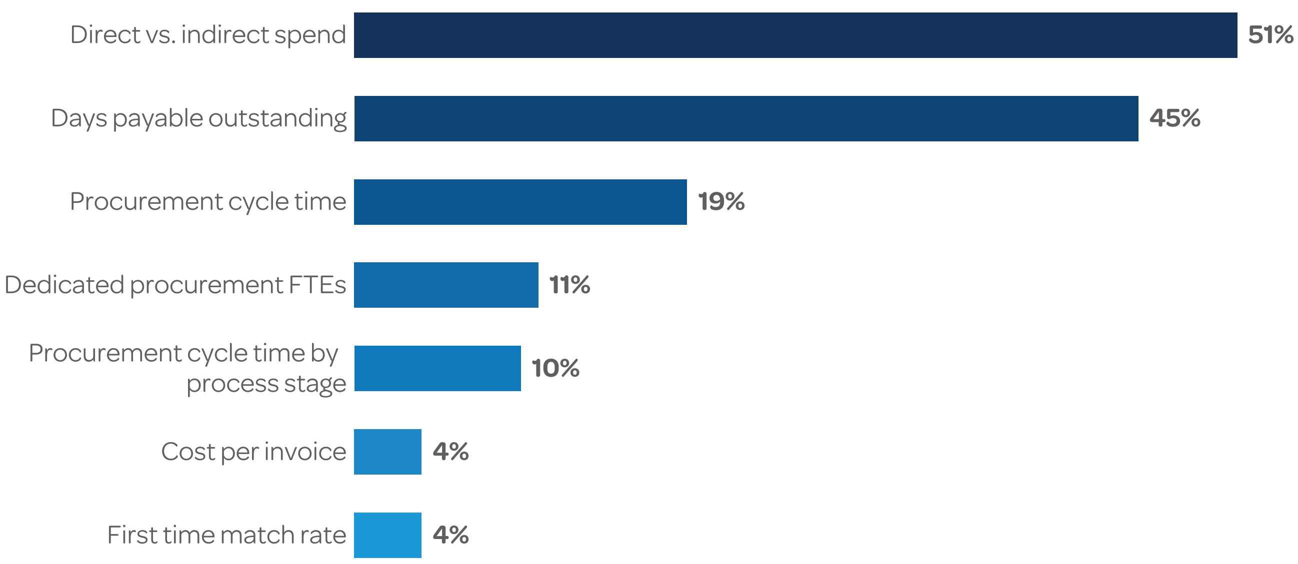
Procurement

Procurement managers are also challenged to maintain continuity with fewer resources available. Headcounts appear to be at a bare minimum, a likely contributor to declining performance and risk management measures. To achieve greater agility and retain customers, leaders intend to address staffing levels in 2021.

And, with twice as many suppliers attached to contracts compared with last year, procurement teams are stretched thin.

Procurement professionals have scaled back on KPI tracking, with the most focus devoted to closely watching cash flow with direct versus indirect spend and days payable outstanding. Little analysis appears to be dedicated to monitoring the procurement cycle time and the procurement cycle by process stage or even dedicated full-time employees.

Tracking Procurement KPIs



272

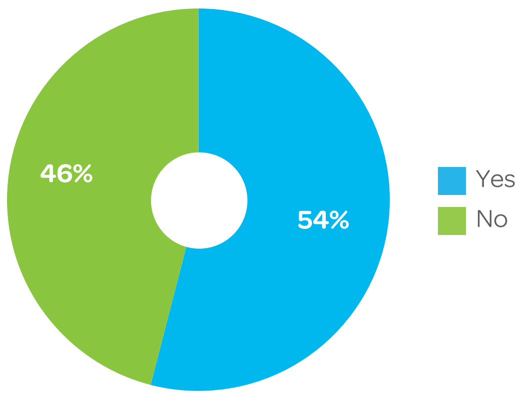
The number of suppliers on contract continues to trend upward, driven primarily by large businesses.

This indicates an evolution toward more complex projects, which appeared to rise dramatically during the period.

Procurement Team Also Manages Contracts

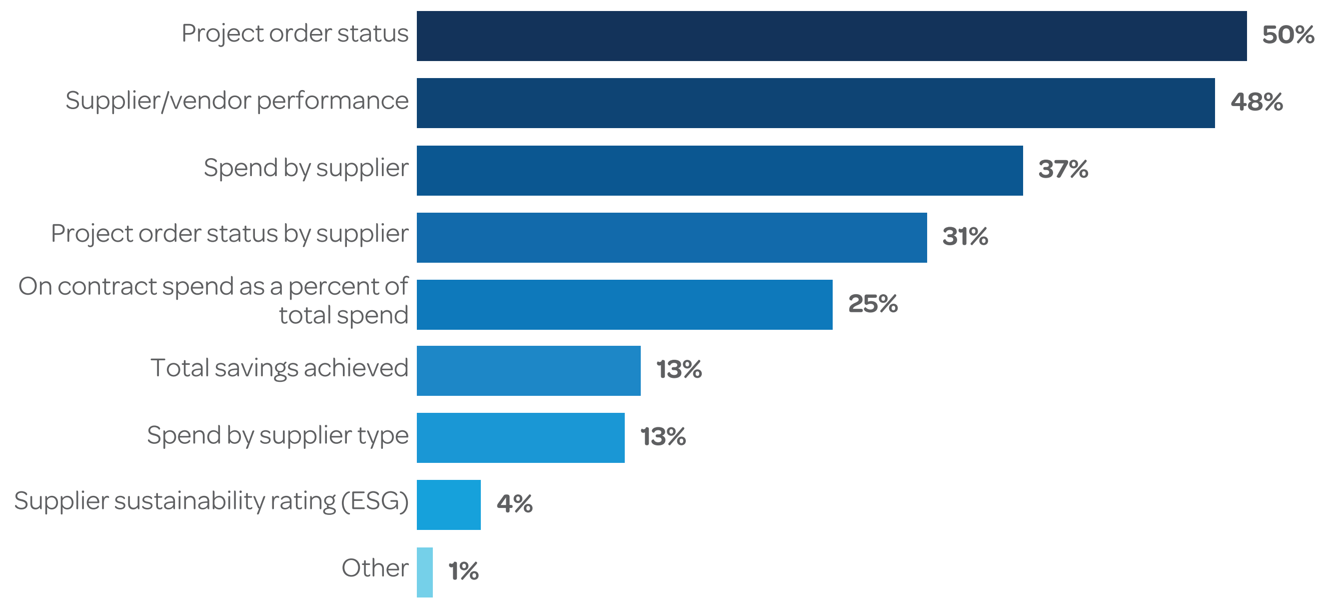
The complexity facing procurement managers is evident in the number of suppliers they now utilize and manage. Large businesses have as many as 1,000 suppliers or more, with small businesses tracking dozens. Similarly, the average number of buyers with which companies work overall is nine, with large-sized companies working with as many as 17. This metric held steady in 2020.

Procurement managers often do double duty managing contracts. The percentage of those doing both jobs rose to 54% in 2020 compared with 48% in 2019. The pandemic likely forced some consolidation of responsibilities as headcounts dropped.



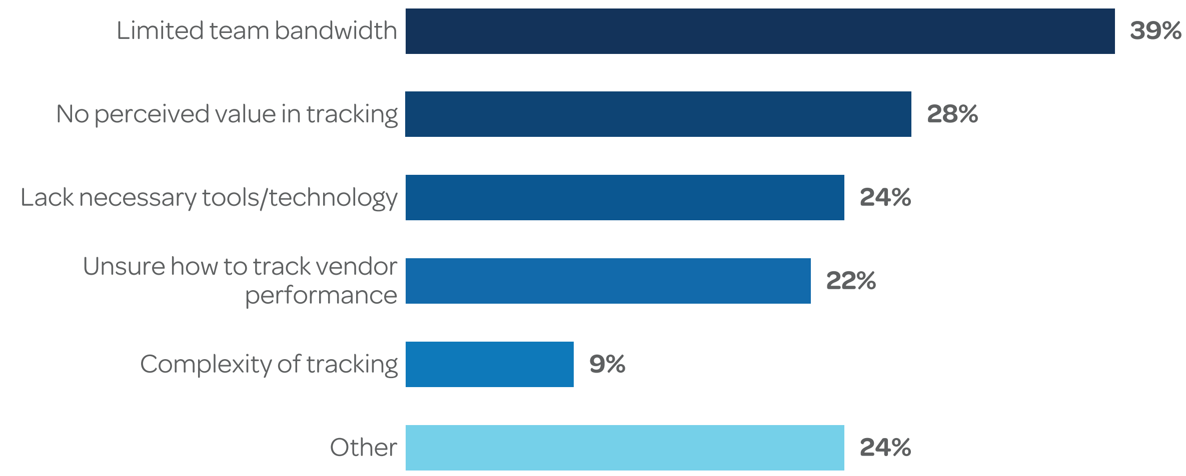
Procurement Metrics Tracked

When managing suppliers, businesses most widely track project order status, (50%), and supplier/vendor performance. Despite a more relaxed review of other KPIs in general, procurement teams retained their focus on spend by supplier as businesses diligently tracked revenue even more closely in 2020.



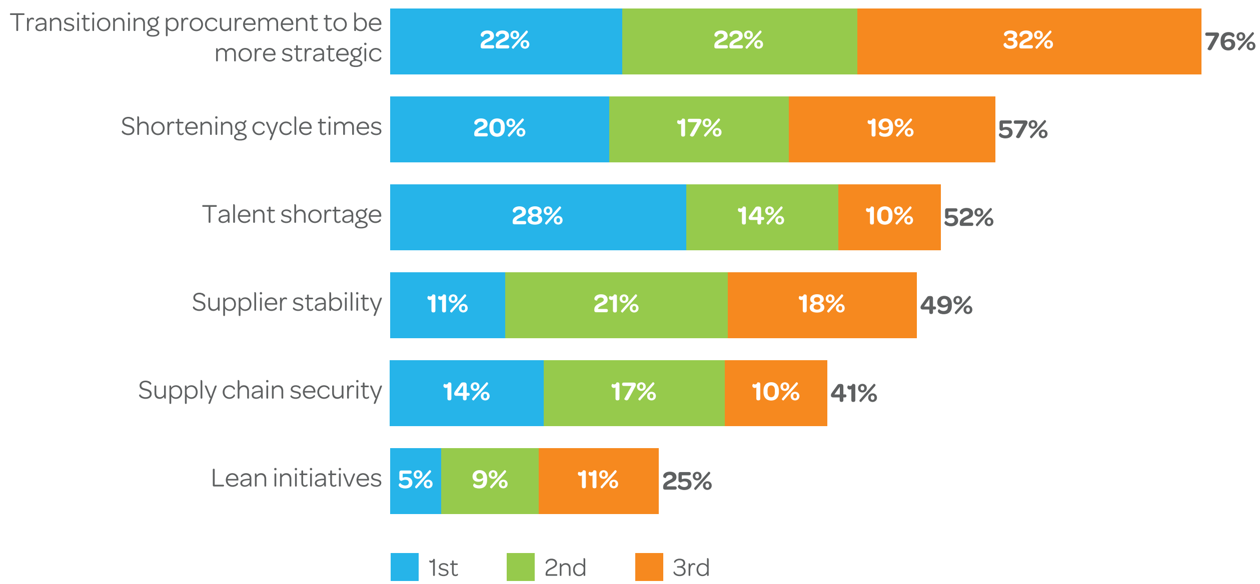
Reasons for Not Tracking Vendor Performance

More than one in four businesses do not track vendor performance, resulting in a missed opportunity. Thirty-nine percent (39%) cite limited team bandwidth, but 28% do not perceive value in tracking. This may be due to the lack of necessary tools/ technology reported by 24%, along with more than 20% that are unsure how to track vendor performance. As procurement teams look ahead to 2021, there will be many opportunities to learn how to integrate tracking measures into their processes.



Top Three Procurement Challenges in the Next 12 Months

Procurement managers intend to be more strategic, which requires having the tools and knowledge to integrate the function into the concerns of the wider enterprise, particularly finance. Seventy-six percent (76%) of respondents named this as a top challenge, followed by shortening cycle time and talent shortage. Shortage of skills is a significant drag on procurement, which could provide real cost savings and efficiencies with the right people and tools



CLARITY OUTLOOK

Contract Management and Procurement

With reduced headcounts, contract management and procurement teams focused almost exclusively on cash flow oriented KPIs. Managing contract suppliers stretched staffs thin. In spite of this, contract management and procurement professionals envision greater access to integrated KPIs to inform strategy as well as support agility.

Companies need to address the shortage of full-time employees dedicated to contract management and procurement in 2021. Importantly, hiring the right employees with appropriate experience and capabilities is key to elevating this function to a higher level of strategic performance. The competition for talent may require a reexamination of recruiting and compensation approaches. Post pandemic, it is likely that competition for talent will intensify.

Providing the right tools to employees is equally important. At this juncture, many still rely on readily available generic tools, when customized software could provide much more comprehensive business intelligence information. Access to the best data facilitates optimum decision making. The growing number of suppliers and complexity of the network demands better tools to measure performance.

SECTION SIX

Information Technology and Cybersecurity

54%

Named operations as the principal focus in 2020. IT professionals continued on their mission to secure data and technology while adapting infrastructure to support customer fulfillment.

A major directional trend in 2020 was the focus on cybersecurity imperatives to protect networks used by a remote workforce. Measures to protect the federal supply chain also gained more focus.

At the same time, companies are investing in efforts to leverage big data to improve insights and inform strategic decisions. Those who succeed early will stand out against the competition. Smaller companies are less likely to lean into tech trends overall, though they too have narrowed focus on big data and data science.

Investments in cybersecurity are starting to show positive returns, as the rate of cybersecurity incidents leveled off in 2020. Across the industry, security and authentication received the biggest investment, which is crucial to sustaining a remote workforce and maintaining compliance.

TOP THREE INFORMATION TECHNOLOGY AND CYBERSECURITY CHALLENGES

1. Maintaining business continuity
2. Leveraging technology to support operations infrastructure
3. Continuing migration to the cloud

Important security regulations are on the horizon, as the Department of Defense (DoD) released requirements for Cybersecurity Maturity Model Certification (CMMC). All Companies that do business with the DoD will have to certify their CMMC compliance by October 1, 2025, which will serve as a go/no go decision in contract awards. Contractors will have to pass an audit performed by a DoD accredited auditor. Approximately one-quarter of government contractors are either unaware of this requirement or unsure what to do.

The process of migration to the cloud does not seem to have been materially impacted by the pandemic. More than 50% of business applications are now in the cloud, but one-third of business applications remain on premises.

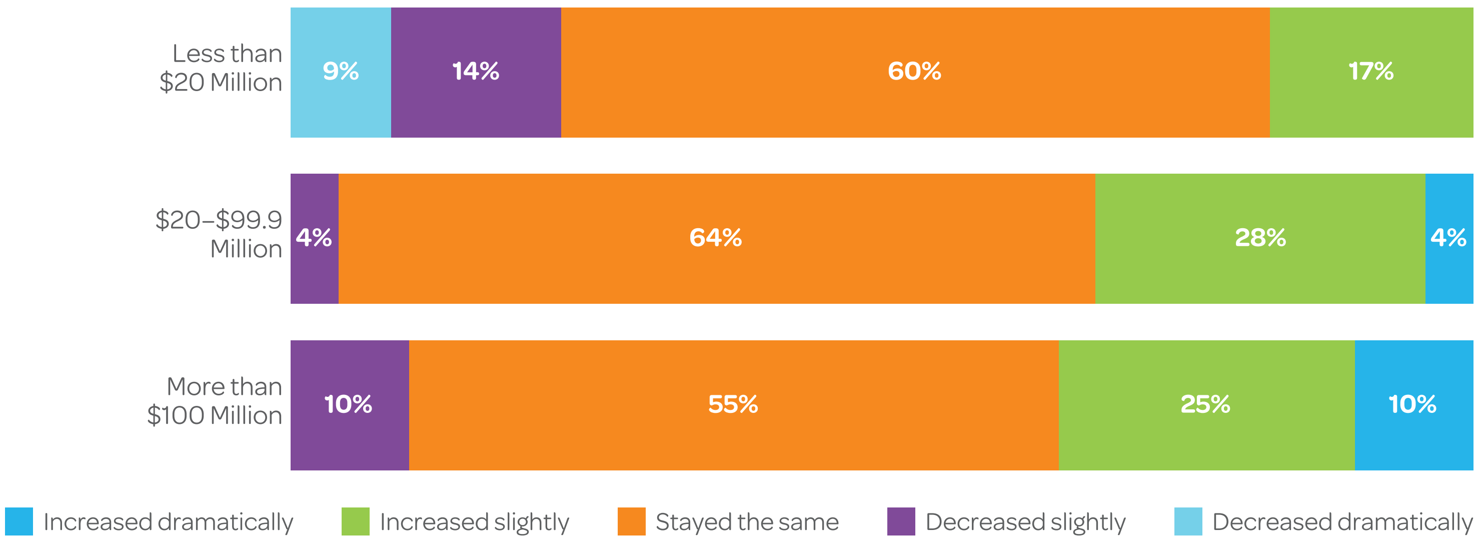
Businesses are using more KPIs and are making them more accessible across their organizations, with expectations for business intelligence holding steady.

As triage to preserve revenue, businesses tightened focus on delivering on client needs while reducing investment in support functions.

Cybersecurity Experience in 2020

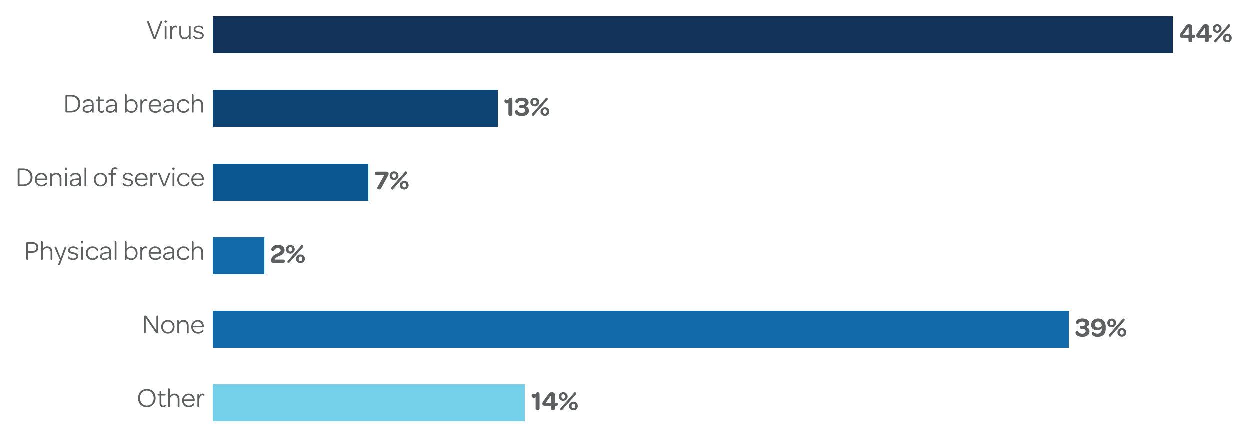
Investment in cybersecurity tools and services is starting to pay off, as the number of cybersecurity incidents declined slightly year over year. Most respondents indicated that the number of incidents had either stayed the same or decreased. New threats, of course, will mandate continued vigilance.

Number of Cybersecurity Incidents



By a wide margin, viruses continue as the main problem among those who experienced a security challenge, rising to 44% from 32% the prior year. Security measures shored up enough to prevent an increase in data breaches; 13% of respondents reported they had experienced one or more. Thirty-nine percent (39%) of businesses indicate that they had no security challenges, which may or may not prove to be an optimistic assessment.

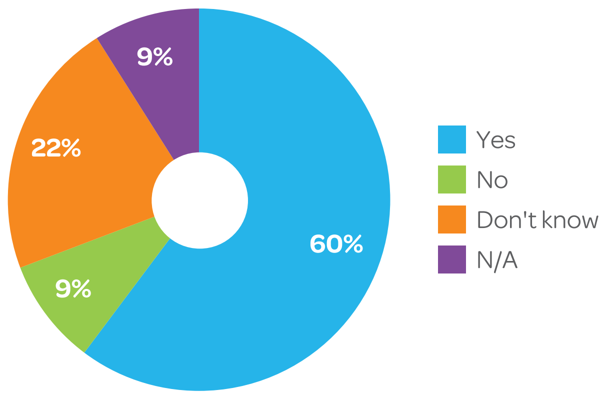
Security Challenges in Past Year



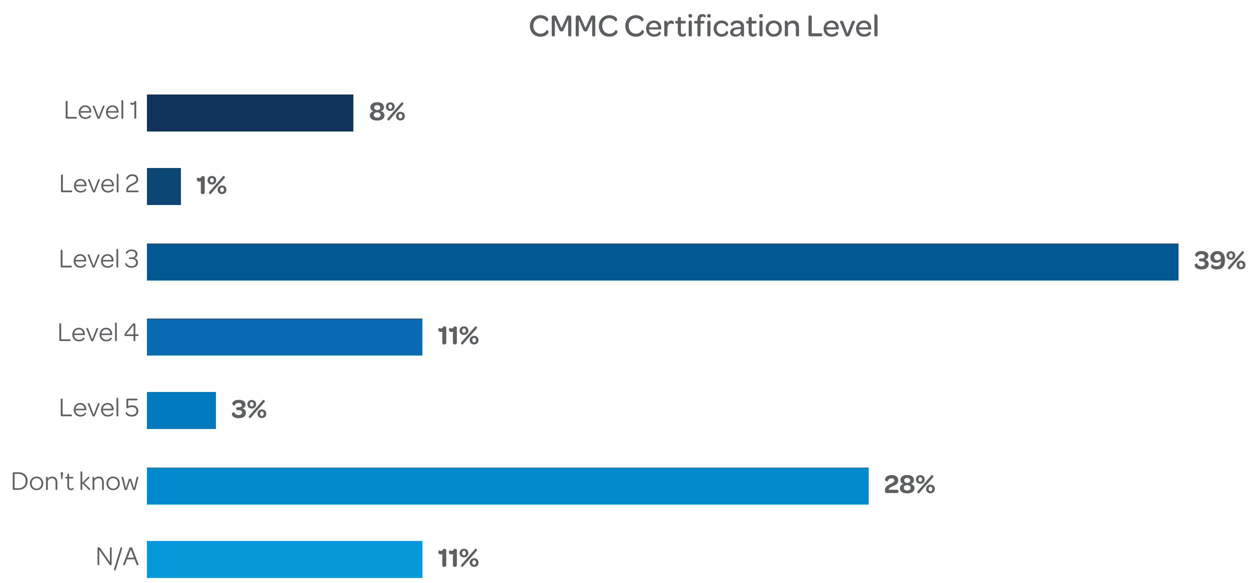
Cybersecurity Maturity Model Certification (CMMC)

Sixty percent (60%) of respondents indicated that they have performed an internal assessment of the controls, policies and procedures required to meet CMMC requirements, which will start on select contracts in 2021. All contractors must comply by 2025.

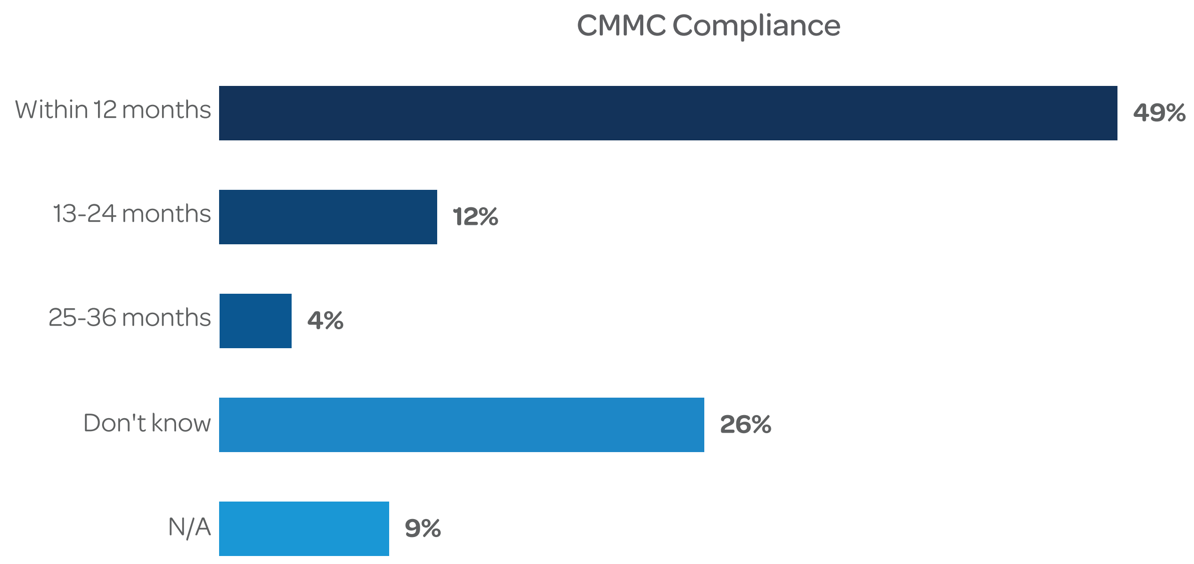
Certification is required for certain federal contracts. Yet, more than 20% of respondents indicated that they are either unaware of or uncertain about this important new requirement.



There are five levels of certification under CMMC. In fiscal 2020, 39% of respondents who were aware of this issue indicated their intention to pursue a Level 3 certification, which closely aligns with NIST 800-171 requirements for handling controlled unclassified information (CUI). To meet Level 3 certification, companies will be assessed on their ability to demonstrate all practices to address Levels 1, 2 and 3. This will include technical architecture and solutions, along with written policies.



Half of those intending to comply expect to do so in the next 12 months while another 12% expect to comply within two years.



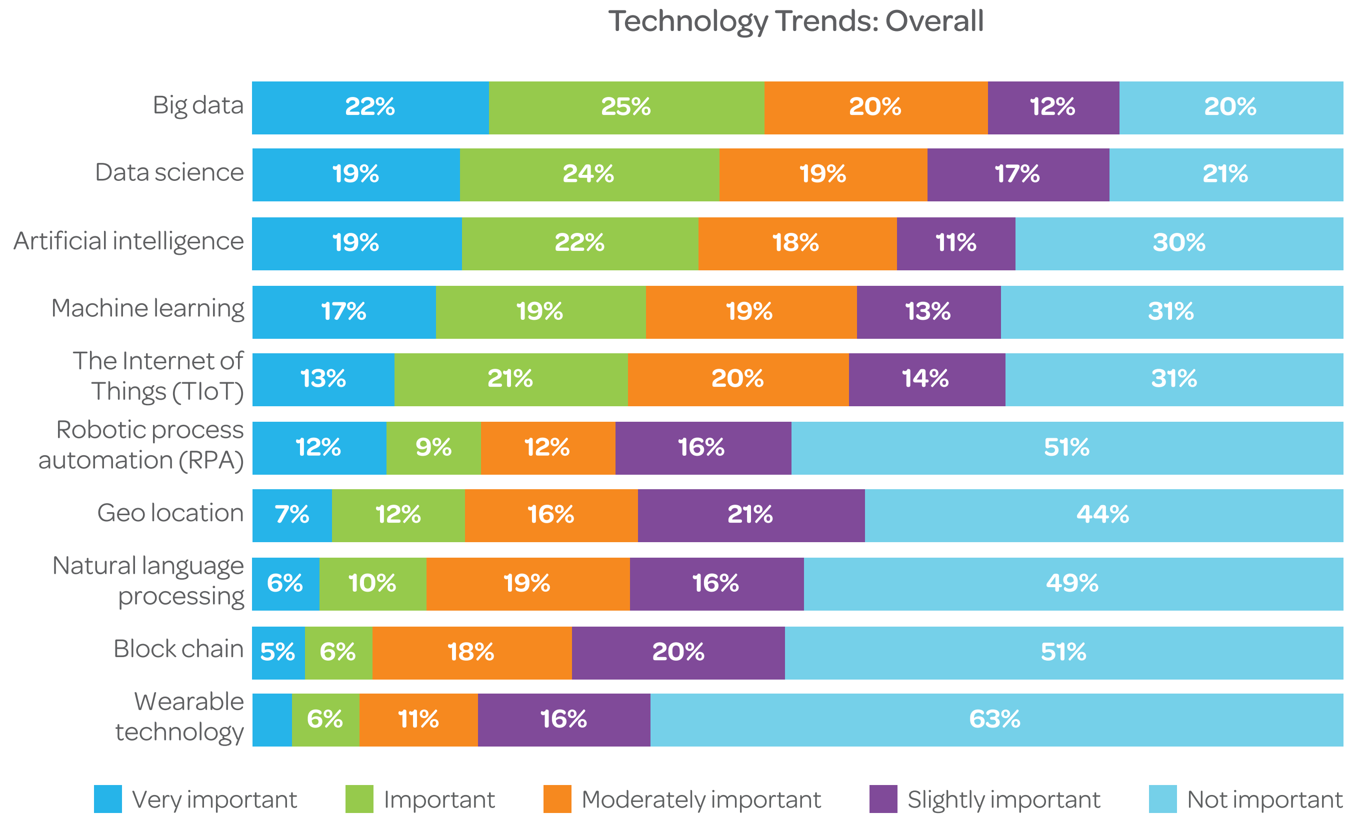
80%

Of IT professionals turned heavily to big data and data science.

Other technology trends took a backseat as businesses directed attention to continuity and cybersecurity.

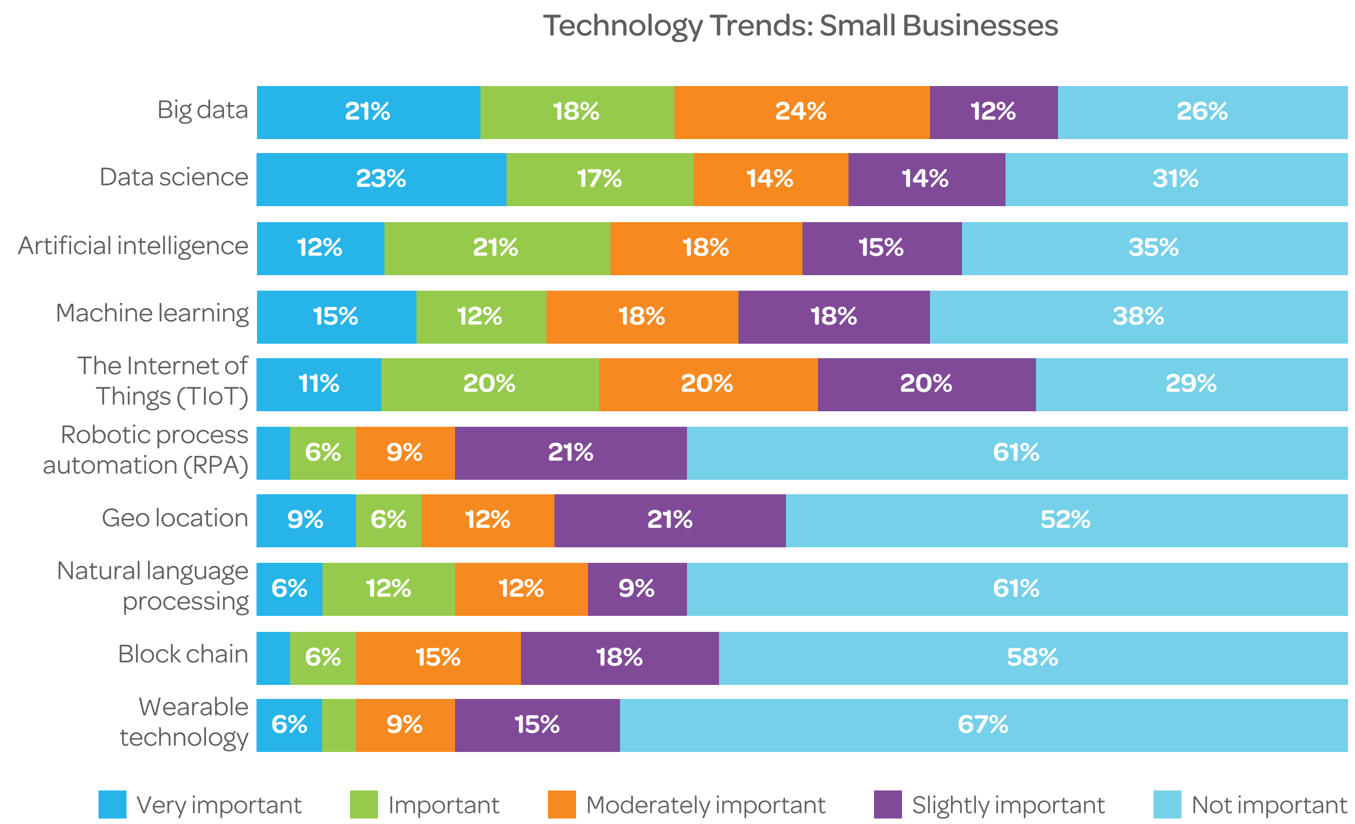
Technology Trends

The most important technology tools remain big data, data science, artificial intelligence (AI) and machine learning. However, an overall decline in investment in these tools likely reflects the urgent focus on other revenue-driving priorities, such as adapting processes to meet customer needs. This is consistent with other downturns, when research and development-focused work tends to get put on hold.



Technology Trends

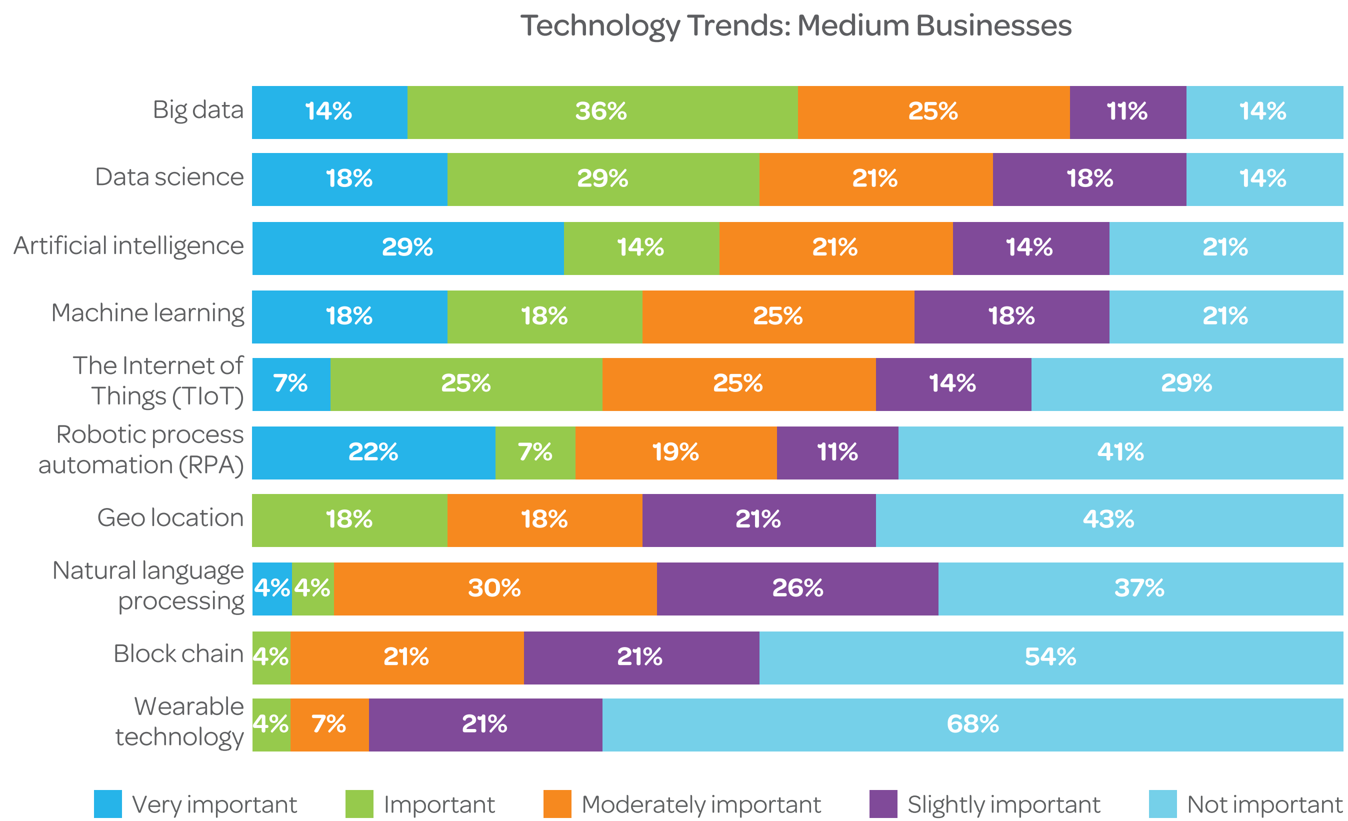
Small businesses focused most on data science and big data while deprioritizing machine learning and artificial intelligence. The level of importance ascribed to matters other than the top two decreased significantly. This may be due in part to the possibility that they are not yet producing actionable results on a broad or profit-driving scale, so efforts in this area may be put on temporary hold.



Technology Trends

Medium-sized businesses are directing their investments toward technology that produces cost-saving assets. Nearly 80% of respondents viewed AI as important to some degree, with 29% identifying it as very important.

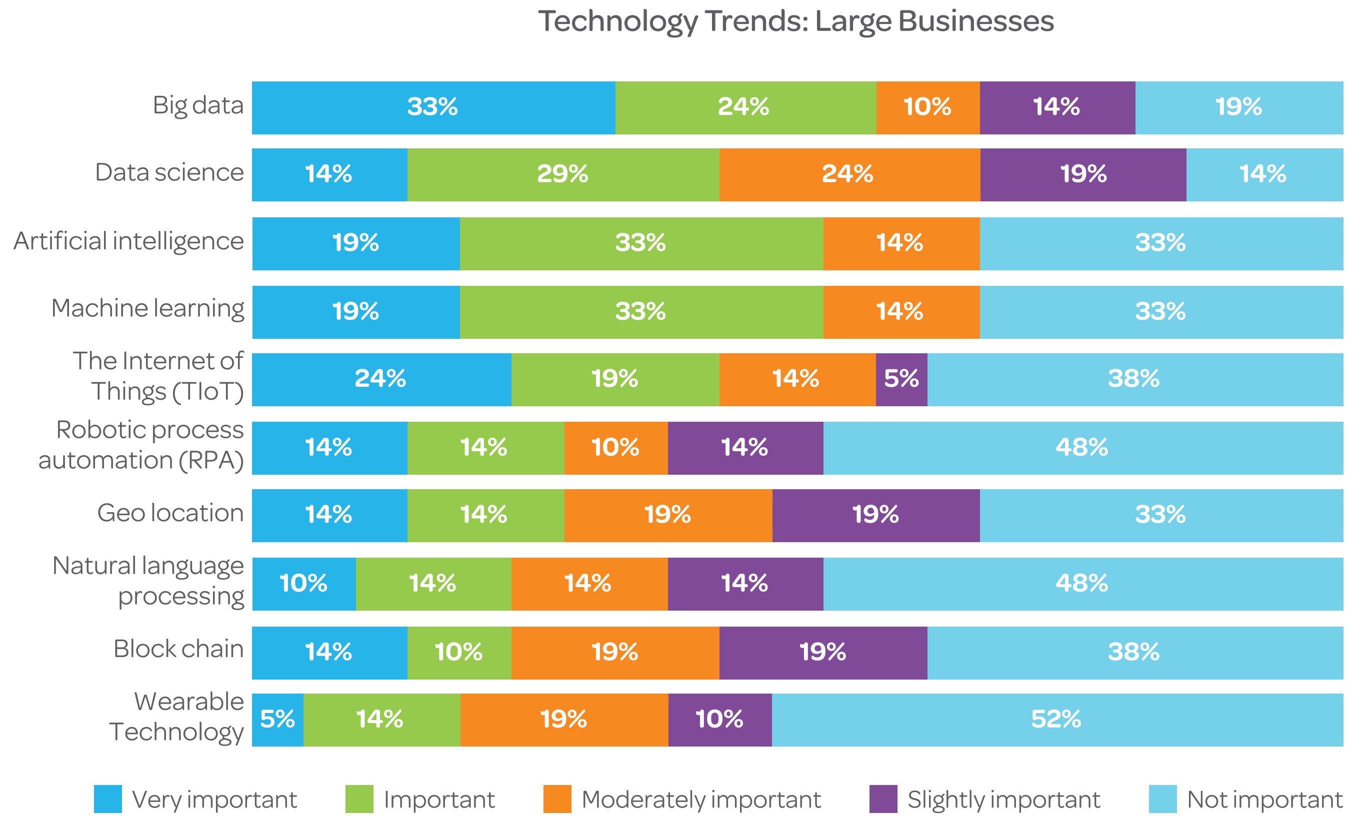
Robotic process automation (RPA) was also of great interest, as companies look for ways to automate repetitive tasks with bots that function like a person. Such automation would free employees for more value-added work.



Technology Trends

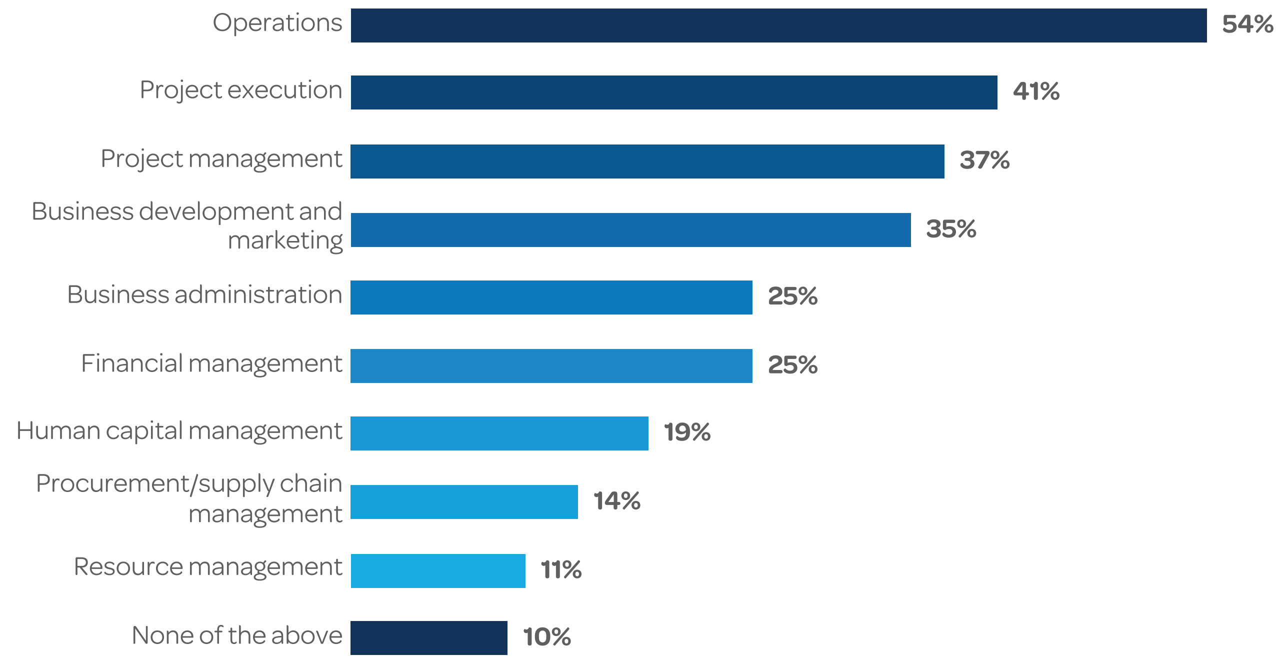
Large businesses did not rate RPA as immediately important, but the federal government is interested in this technology and many large consulting firms have started practices specializing in it.

During the pandemic, large businesses tightened their focus on big data and The Internet of Things (TIoT), which may reflect investment in internet-based communication and collaboration tools for a remote workforce.



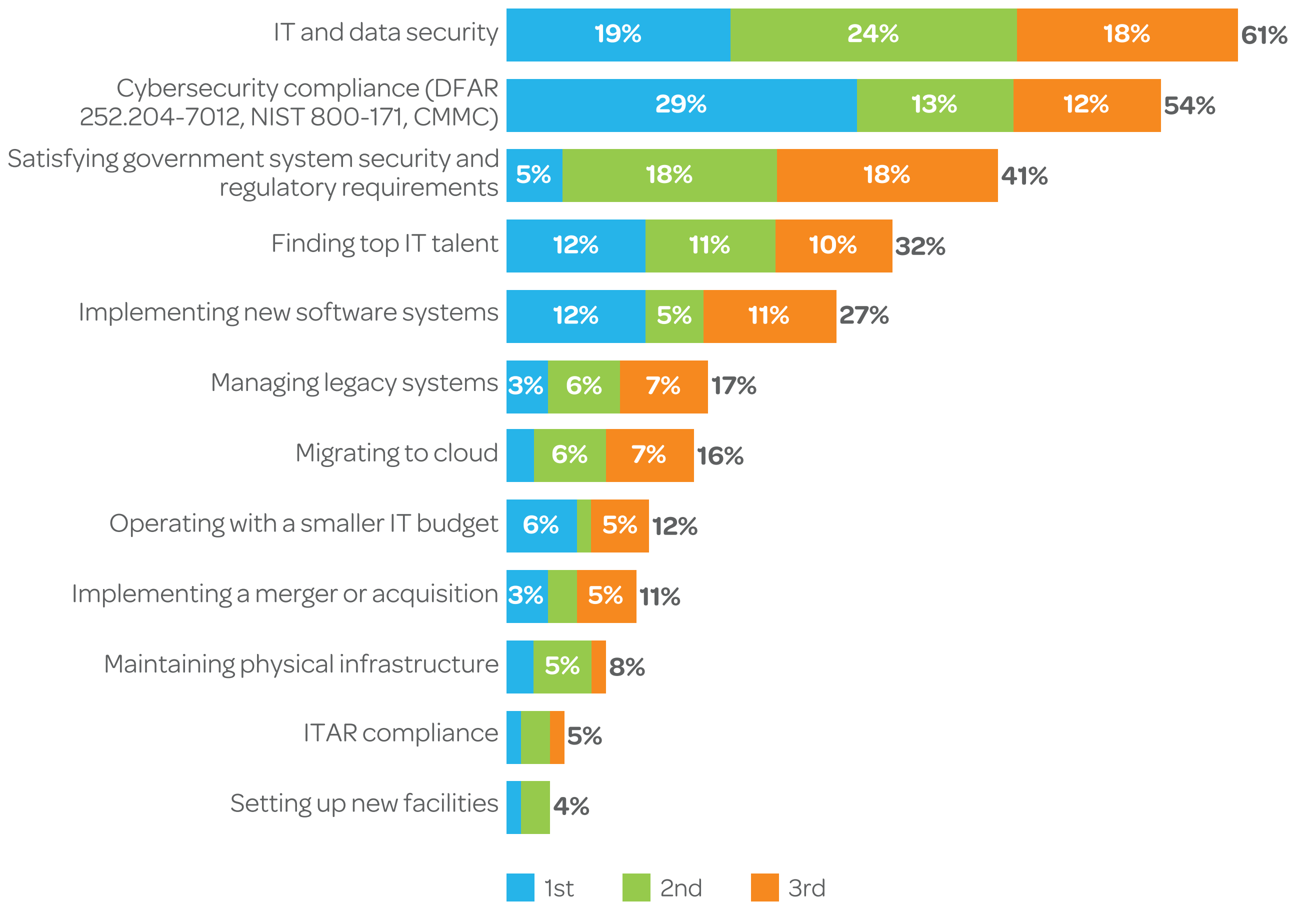
Applying Technology Trends

In 2020 business concentrated the application of technology trends into operations, while retaining focus on project fulfillment and sales. Leveraging technology for infrastructure to buttress support functions was a lower priority relative to driving, capturing and maintaining revenue.



Top IT Challenges

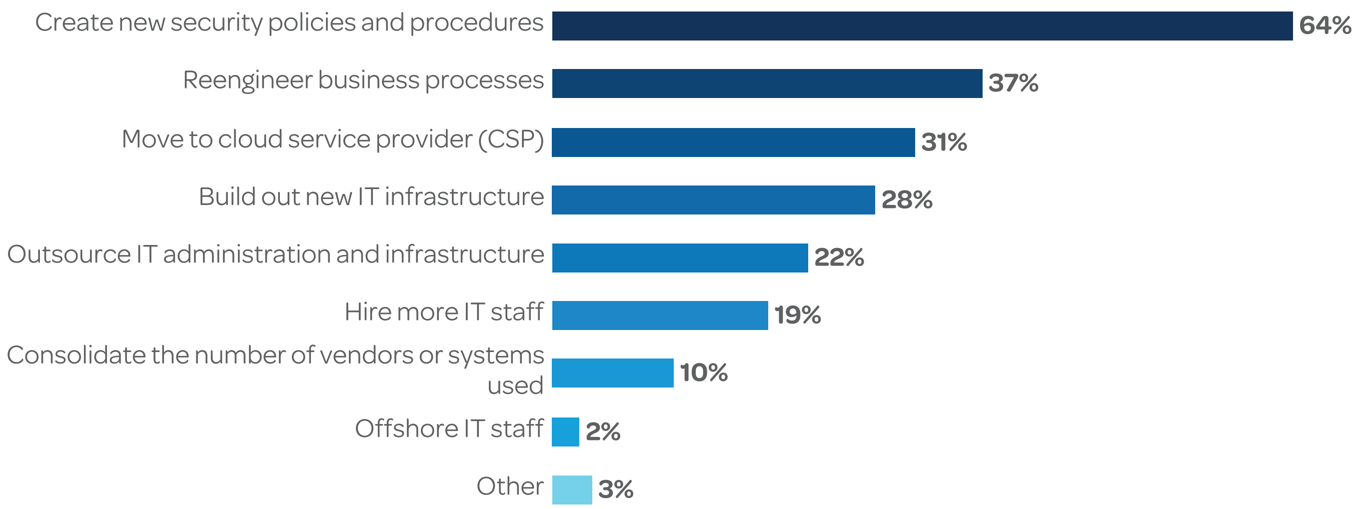
IT, data security and cybersecurity compliance were hot buttons in 2020. The necessity of a largely remote workforce required even greater attention to data security, while the impending requirements of CMMC loomed large. Fifty-four percent (54%) of Study participants named cybersecurity compliance as one of their top three concerns.



Addressing Top IT Challenges

Businesses continue to prioritize the implementation of new security policies and procedures to address the top IT challenges. Companies seek to do more with less by moving more functions to cloud service providers (CSPs). This does not eliminate the need for dedicated staff but can free them for other more strategic initiatives for the organization.

Businesses did not generally seek to hire more IT staff. Rather, they looked to reengineer business processes.



CLARITY OUTLOOK

Information Technology and Cybersecurity

Companies are increasing use of business intelligence across multiple functions to improve processes and the bottom line. From cloud-based solutions to big data and data science, IT professionals are leveraging these tools to drive more efficient, safer business practices. Sustained levels of investment in cybersecurity and compliance are on the horizon for 2021 and beyond.

Compliance requirements will continue to promote migration to the cloud, which will result in cost savings and greater efficiency. Those applications (one-third) that remain on premise should be re-evaluated and assessed for migration potential.

As migration of applications continues, the role of IT professionals will evolve from executors to strategists. Their jobs will shift toward monitoring trends, adopting new technologies and looking for ways to utilize technological tools for competitive advantage.

Cybersecurity will remain an area of major focus, as continued threats materialize, and bad actors use new methods of infiltrating networks. CMMC requirements will garner significant attention and time from companies that wish to be included on certain federal contracts, as those that don't meet the requirements will no longer qualify.

Summary

Government contractors overall successfully navigated a challenging year. By maintaining a keen focus on the fundamentals, business continuity and meeting customer needs, contractors were able to thrive during a difficult period. The outlook for 2021 is bright as revenues are expected to grow and the effects of the pandemic recede.

While contractors did experience lower contract values and delays in 2020, these effects of the pandemic are expected to lessen moving forward. Additional challenges resulted from a sharp shift to a virtual workplace, but companies adapted and learned how to manage and work remotely. The lingering effects of virtual workforce policies could greatly expand the range of available talent and facilitate successful competition for new hires as companies would no longer be limited to certain geographies.

2020 also saw companies prioritizing "must-have" investments like business development and project management.

A renewed focus on risk management or investment in cutting-edge technologies, like artificial intelligence and machine learning, will promote long-term success with better predictability and metrics. Investment in new tools also took a back seat in 2020, which is expected to right itself in 2021. Taking advantage of the best tools and software will set successful companies apart.

Companies will need to continue to focus on fundamentals going forward and strategically invest as the effects of the pandemic begin to fade.

Statistics at a Glance

		SMALL	MEDIUM	LARGE
BUSINESS DEVELOPMENT				
Percent Prime Contracts (Average)		48%	63%	72%
Percent Subcontracts (Average)		52%	37%	28%
Win Rate (Median)		43%	34%	40%
PROJECT & RISK MANAGMENT				
Change Order Win Rate (Median)		75%	63%	50%
EAC/ETC Forecasts (Median)		80%	90%	90%
Projects On or Under Budget (Median)		90%	90%	88%
Projects On or Ahead of Schedule (Median)		75%	80%	85%
Schedule Risk Analysis (% of Organizations by Phase)	Bid/Proposal:	37%	50%	67%
	Initiation Phase:	37%	28%	43%
	Execution Phase:	42%	50%	67%
	Not at All:	26%	13%	10%
FINANCIAL METRICS				
Change Order Win Rate (Median)		75%	63%	50%
EAC/ETC Forecasts (Median)		80%	90%	90%
Projects On or Under Budget (Median)		90%	90%	88%
Projects On or Ahead of Schedule (Median)		75%	80%	85%
Percent Subcontracts (Average)		52%	37%	28%

Statistics at a Glance

	SMALL	MEDIUM	LARGE
CONTRACT MANAGEMENT AND PROCUREMENT			
Percent Using Contract Management Software	4%	26%	29%
Days Payable Outstanding (Median Days)	38	30	28
HUMAN CAPITAL MANAGEMENT			
Training Spend per FTE (Median Dollars)	$265	$150	$300
Composite Turnover Rate (% Over 10%)	25%	34%	67%
Time to Fill Position (% 60+ Days)	10%	23%	31%
INFORMATION TECHNOLOGY			
Percent of Apps in the Cloud (Median)	65%	71%	45%

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- Track thousands of federal, state and local contracting opportunities
- Leverage actionable intelligence on market trends
- Improve contract win and retention rates
- Complete projects on time and under budget
- Ensure project, information technology and corporate governance
- Streamline the financial management of their organizations.

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