



DCFL Insights

Facilities management sector in UK

Facilities management is a multi-faceted profession, which has been created out of a need to provide professionally managed and critical support services.

Overview

Facilities Management (FM) includes a broad spectrum of services, from 'hard' (such as building maintenance) services, to many 'soft' (such as security and cleaning) services that are contracted out to third party companies. Examples of facilities management include Catering, Technical, Security, Cleaning as broader heads. It includes services like building maintenance & services, guarding, office cleaning, waste cleaning, reception, security, mechanical and engineering, storage and landscaping.

The market for UK facilities management sector has grown to £106.3 billion in 2012 and is forecasted to reach £117.2 billion by 2017. That is a 9% increase in FM services contracted out and 17% growth in take-up of total FM (TFM) services.

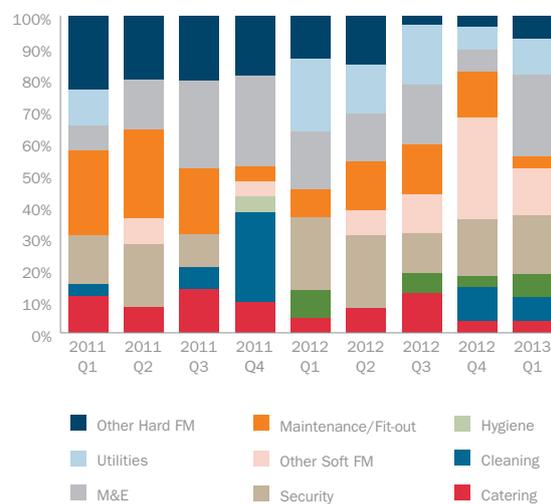
M&A in 2013

The flow of mergers and acquisitions in the UK's FM sector remains robust despite the wider issues in the economy as a whole. In total 27 FM deals were announced during the first three months alone of 2013.

There is evidence of a rising trend in M&A volumes per annum since the 2008 economic slowdown, with growing interest from foreign buyers. Almost 500 UK FM corporate finance transactions were recorded over the five years to 2013, with 2011 recording the highest annual level of activity. 2011 recorded around 100 FM transactions in the UK, however 2012 figures were somewhat lower, with around 95 transactions taking place in this space during this period.

In terms of specific FM markets, until the final quarter of 2012, the 'hard' space has been most active, particularly the M&E and building services market. In the last two quarters, activity in the security, cleaning and other soft FM sectors have swung the balance away from hard FM in numerical terms. Q1 2013 witnessed a sudden jump in deals being announced in the M&E sectors and boosted the hard FM almost back to parity.

UK Facilities Management transactions by subsector 2011-2013 by quarter



Deals

In 2011 Linbrook Services Limited (a leading provider of responsive repairs and maintenance services to the affordable housing sector) were acquired by Wates Group Limited. Market consolidation has seen many large FM groups bolster market positions, such as Carillion plc's acquisitions of Mowlem and EAGA and Compass Group's acquisitions of VSG and ICM.

2012 deal flow include India's TOPSGRUP, a leading Indian security group, which announced the completion of the remaining stake in British security firm, The Shield Guarding company, valuing Shield at £32 million. Rentokil Initial plc's acquisition by its Initial Facilities Division of London based technical facilities management business Modus FM was another transaction that brought additional technical services capability. LDC recently backed management in its bid for Airline Services Holdings, a provider of a range of services in the area of aircraft presentation and cabin interior, reportedly valuing the business at over £30 million.

One significant transaction during the first quarter in 2013, came in the form of Ferrovial's £385 million bid (via its UK subsidiary Amey plc) to acquire Enterprise Group Holdings, the provider of utilities infrastructure maintenance, from private equity investor 3i.

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The Enterprise Group Holdings deal also highlights the continuing trend towards M&A involving international entities as buyers. Six such deals were announced in Q1, bringing the total in the 12 months to the end of March to 19.

Prospects

FM groups will continue to be selective in the assets they acquire. Strong valuations will be achieved by only the highest quality FM assets, which offer genuine differentiation from their peer group and are capable of making a real and immediate difference to the buyer. Additionally, many of the key deal drivers in FM are underpinned by a variety of defensible qualities that these companies have, such as resilient end-markets and good earnings visibility. With such forces in mind, strong transactional activity in the FM sector is expected to continue for the foreseeable future.

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Private equity

Apart from the strategic markets in this space, private equity investors have historically been active in FM. Unlike many sectors in which private equity operates, the highly fragmented nature of the FM market lends itself to the buy and build strategy, where a 'platform' business is acquired to be supplemented by further acquisitions to create scale. Lyceum Capital has implemented this strategy in the drainage services submarket with portfolio company UKDN Waterflow, the UK's largest independent (non-franchised) specialist drainage contractor. Since Lyceum Capital backed UKDN in January 2010, UKDN more than doubled its turnover to £55 million.

The current activity by private equity investors is on a lower side with financial buyers hamstrung by the difficult leverage conditions and showing little ability or appetite to compete for targets. The 12 months to the end of March 2013 saw just nine deals backed by private equity houses as compared to 25 in the same period of 2007/08.

Public markets

Some of the key players in this domain are Compass Group plc, G4S plc, Serco Group plc, Rentokil Initial plc, Balfour Beatty plc, Berendsen plc, Carillion plc, Mitie Group plc, Interserve plc, Kier Group plc, Mears Group plc, London Security plc, May Gurney Integrated Services plc, Johnson Service Group plc, ISG plc and Green Compliance plc.

Future trends

With value, rather than volume growth being the key watchword in the UK facilities management market in 2013, FM providers are currently finding success through the use of tactics such as more closely matching service provision to the client's corporate aims, objectives and culture. This 'strategic integration' offers good opportunities for value growth in the near to medium term. One important trend in UK facilities management market is that the cost pressures and skill requirements is further driving M&A in this sector.

The continued trend towards outsourcing is expected to ensure future growth opportunities for FM companies, with bundled services and strategic solutions in particular showing the strongest growth potential.

On the downside, many are achieving higher turnover but at lower margins as significant pressure on cost-reduction is set to remain a feature of FM contracts.

There is also an ongoing trend of large single service providers merging with organisations which have a different skill set in order to diversify. We can see that FM companies are pursuing 'strategic FM', adopting a more partnership-based approach and providing more tailor-made services, including the operational management of services and the control of budgets. For example, large FM groups such as Rentokil Initial plc are building capability to capture multi-service contracts where efficiency is seen as key.

Multi-service FM has grown share to more than 30% of the UK FM market in 2013 and it has come to the notice that there is an apparent growing level of disillusionment with some 'bundled FM' service providers. This appears to be a growing trend in the FM industry with clients increasingly suggesting that some multi-service providers are unable to live up to expectations in terms of providing better value for money or level of service than single service providers.

Thoughts.....

Different research studies have different views about the sector. Some consider it to be a relatively new sector while others say that this is a mature market and doesn't have much potential now. The sector faces up to the challenge of a long and slow recovery. Consolidation may help build strong players with less competition. Quality, client delight and efficiency would be the primary attributes for survival and growth here.

FM companies can now focus more on new verticals, and areas such as healthcare and education, which have been in the spotlight recently with many acquisitions happening in this space in UK recently.

International expansion will play a central role in the strategies of many domestic FM businesses. Many of the larger FM players are moving their focus on international expansion as an option. Serco, for example, has managed to offset losses sustained as a result of public sector cutbacks, both in the UK and the US, by securing a record £5.8 billion of new global contracts in 2012. It now generates more than 45% of its revenue outside of the UK – up from 40% in 2011. In summary International expansion will play a huge role in growth in FM for 2014 and beyond.

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