clearthought

Facilities Management

Leading players have been busy enlarging their portfolio of services and becoming strategic service providers

Global horizons

As companies place an increasing focus on cost reduction and core competencies, the FM industry has gained increased significance across a swathe of sectors.

Leading players in the industry have seen M&A as a central way of fulfilling their wider corporate strategies. On the one hand, they have embarked on aggressive acquisition strategies in order to exploit new service lines and increase their geographic coverage. On the other, some operators with a background in commercial property are retreating from the broader FM sector and divesting of non-core services.

Rise of multi-services

Many FM firms started out providing a single-service local offering, often focused around basic cleaning and maintenance. However, as clients began to fully grasp the financial savings and the opportunities to transfer risk that came from outsourcing, FM companies quickly expanded their propositions to provide a bundled service offering.

This enlargement in the portfolio of services has been a key source of growth for leading players and, more recently, the model has developed further so that FM companies act as strategic partners rather than just service providers.

This approach, known as Integrated Facilities Management (IFM) or Total Facilities Management (TFM), centres on providing more value-added services, often with a level of risk exposure and performance-based contracts, and is increasingly being seen across Europe.

At the same time, technology has played a significant role within the industry via the use of GPS, motion sensors and web-based booking systems. Indeed, FM companies have been reshaping their operations over the last few years as they target higher margin service lines underpinned by technology. This also acts as an opportunity to provide an enlarged service proposition and to cross-sell, further driving the growth of the IFM market.

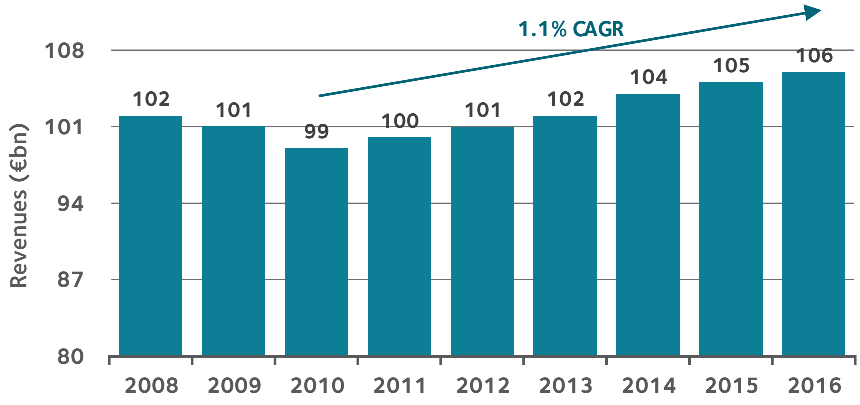
Growth prospects

As the table below illustrates, market growth in the sector has been modest in recent years with fairly paltry levels of annual growth.

However, the overall figures mask the fact that specific sub-sectors such as energy management and security have become highly-specialised, value-added platforms that can provide strong returns to investors which might otherwise be deterred by the relatively low margins, low growth and high churn of FM soft services and low value-add M&E contracting.

Indeed, investor appetite for tech-enabled FM companies delivering high margin services to a robust end market remains strong.

European outsourced facilities management market



SOURCE: Frost & Sullivan

Industry trends

Integrated Facilities Management (IFM)

Unlike the bundled service offering in which the FM company acts as a supply chain manager, the key to IFM is that services are self-delivered and cross-utilise employees across different functions.

In doing so, this helps to ensure services are not performed or managed in silos – a criticism often levied against the bundled service approach.

Leading multi-services FM players include Samsic, Compass, Mears, Mitie, Interserve, ISS, Facilicom Services Group, Carillion, Aramark, Sodexo, Rentokil, ABM Industries, Amey, Servest, OCS Group, Kier and CBRE.

The rise of IFM is particularly noticeable in the UK market which has been at the forefront of developing the model.

Large contracts

IFM tends to suit larger international clients or large public sector contracts that require geographical reach or which can benefit from greater economies of scale.

For instance: Mitie, which was originally founded as a cleaning business, is a good example of a FM company that has followed an aggressive acquisition strategy to enter a number of higher margin, value-added, tech-based services.

Back in 2012, the business entered the energy management space through the acquisition of Utilyx – a sector where clients have experienced dramatic cost rises. In light of this, FM companies have developed energy services that cover strategic planning, procurement and risk management, often utilising a range of sophisticated technology to manage the ongoing consumption of energy. Other areas Mitie has targeted include online criminal records checking services, pre-employment screening and risk management consulting.

Another leading European player is the French group Samsic which, since starting out as a cleaning company, has acquired several service companies across Europe, most recently UK competitor JPC Cleaning Services.

One reason Samsic has looked further afield is that its home market is still relatively undeveloped, as French companies are often still keen to retain full control of real estate assets. They also fear undermining their broader identity by externalising parts of their workforce.

New entrants

Commercial property agents are becoming increasingly active in the IFM market as they look to service their portfolios rather than give margin away. The best example is CBRE, whose purchase of Norland Managed Services in 2013 gave it the ability to self-perform building services in Europe, developing its existing self-delivery capabilities in North America, Latin America and Asia Pacific.

Margin pressures

In recent years, the FM industry has seen intense competition in certain standardised service lines which has led to the continued erosion of margins.

The larger FM players providing a TFM offering are able to benefit from economies of scale and bundle basic low margin service lines as part of a larger offering. However, FM providers focused on low margin core services have struggled.

This is not to say that there is not a role for smaller FM operators, particularly in the SME market which tends to focus on single sites. However, the key for these providers is to focus on specialist services in niche markets where technical expertise is valued above low cost service provision.

Another challenge for FM companies is that contracts are negotiated over many years and prices invariably set up-front. However, business plans can then be side-tracked by unforeseen changes in costs.

A good example is the new National Living Wage (NLW) in the UK which has set an effective minimum wage of £7.20 (€9.05) and which will have a significant effect on FM sub-sectors with a large proportion of low paid workers. Proposed changes to France's labour laws to bring them into line with the more flexible arrangements that exist in other European countries could also have a big impact, although the proposals are facing strong opposition.

European contrasts

Markets across Europe have witnessed notably different rates of growth in recent years.

For instance: the Spanish FM market is now growing again after recent declines, reporting 1% growth to €26.6bn in 2015. The cleaning sector accounts for 35% of the market and the main companies are expanding their portfolio of services due to growing demand for global services.

However, Scandinavia – one of the front runners within FM – has experienced high and stable growth rates, even during the financial crisis, while there is increasing demand for IFM services.

In more mature markets such as these, growth is being secured through an increased focus on delivering value-added services. As a consequence, the market has split between large FM companies capable of delivering complex IFM solutions and a large pool of small service providers which handle simpler services.

In Germany, the FM industry remains a cornerstone of the economy accounting for €205bn of real estate management volume and employing more than four million people. However, the aggressive consolidation strategy that was once pursued by leading players such as Bilfinger and others is now being reversed as key players sell off their commodity FM activities and focus more on sophisticated services or exit the market entirely. Despite the commodity FM market still being very fragmented, PE are hesitant to invest, instead focusing on the higher value-added end of the spectrum.

The Irish FM sector continues to grow as the market matures. Historically, only 45% of FM services were provided by external service providers in Ireland – this is well below the UK average of c. 60% and points towards more scope for growth in the market. Large international players with a presence in Ireland, such as Aramark and Sodexo, as well as domestic operators like Noonan are continuing to develop their scope of services to include higher value offerings in response to this growing demand.

Energy driver

Energy performance remains a key driver of activity within the FM sector and is at the heart of increased value-added strategies. For instance: in the French market, players such as Dalkia are now focusing almost exclusively on this sector. The company recently acquired Cesbron, an expert in commercial refrigeration and HVAC, a move which allows Dalkia to expand its range of offerings to industrial and commercial customers.

Other notable deals include Mitie's aforementioned acquisition of Utilyx and Carillion's purchase of Eaga, a UK company that supplies energy efficient products.

A growing emphasis on working environments and workplace health issues has also been a particular driver, as firms adopt more complex buildings in terms of automation, digitalisation and energy use.

M&A Activity

Over the last few years, there has been a striking divergence in the M&A strategies of players in the FM industry. Some companies, particularly those whose roots lie in the property industry, have been divesting FM divisions, deeming them to be non-core.

These companies originally invested in the market because of the stability of longer-term contracts and the more predictable earnings offered by FM in the wake of the economic crisis. In addition, it allowed construction firms to service the full life cycle of a project by covering the design, build, maintenance and operation of a building through one tender.

Divestments are in part being driven by the intense margin pressures that some FM companies now face, which has led to revenues rising at the expense of margins, as well as an uptick in the wider construction industry. The proceeds from divestments also represent an opportunity to pay down debt and build resource in order to consider future acquisitions that more closely align to the company's core services.

For instance: in the UK, Willmott Dixon put its Willmott Dixon Partnerships and Willmott Dixon Energy Services divisions up for sale, while Bilfinger of Germany is seeking a buyer for its Building and Facility division. Bilfinger was one of many German companies which launched aggressive consolidation strategies a few years ago, but this trend is now being reversed as key players sell off their lower margin, high churn FM activities.

However, there are still plenty of FM players keen to consolidate their IFM offering, often picking up the assets of those very FM players which are retreating from the market.

Cross-border activity

Larger players in the FM market are focusing on expanding internationally as opportunities in their home markets dry up. There is a particular emphasis on emerging markets as well as diversifying into new service lines to provide a total FM solution in response to client needs.

Integrated service capability and geographical reach are becoming important ways to consolidate the supplier base and achieve internal cost saving targets for large international clients. FM players are having to react to client demands becoming more sophisticated and output-driven in developed geographies, while in emerging markets the industry has begun a long-term process of professionalisation and consolidation.

In the very mature UK market, leading FM players are now turning their gaze overseas to fuel future growth, while investors from India, South Africa and the US are showing increasing interest in the British market. Part of the reason is that they have been capitalising on a weak pound and buying businesses at comparatively cheaper valuations, but it is also because companies such as Servest, ISS and Sodexo are using M&A to extend their global reach.

Recent deal highlights

- Spie, a European leader in multi-technical services in the energy and communications sectors, acquired Numac, a leading service provider in the field of industrial maintenance in the Netherlands.
- French company Samsic acquired Serbian FM company Eko Poslovi which has operations across the Balkans. It is the latest acquisition by a French player in the region in the wake of Atalian's purchase of Mopex.
- ISS A/S acquired the UK and Ireland technical services division of GSH Group.
- Derichebourg of France acquired the Portuguese company Safira, a leading provider of waste services.
- CBRE bought the Global Workplace Solutions unit of Johnson Controls Inc, to add to its corporate services business and build on its previous purchase of technical services FM provider Norland Managed Services.
- New Delhi-based facilities services provider Tenon Group acquired multi-service provider Office and General Group Ltd.
- US-based ABM Industries Inc acquired soft services provider GBM Support Services and, more recently, also bought Westway Services, a provider of technical engineering services.
- Chequers Capital-owned ID Verde SAS has been particularly acquisitive. The group recently announced the acquisition of Quadron Services, a specialist ground maintenance company working for local authorities. The deal follows the French group's purchase of The Landscape Group in 2015.

Private Equity

The FM market has traditionally been attractive to PE investors for a number of reasons:

- Positive long-term trends in the market
- Historically good exit opportunities on public markets and strong appetite from corporate buyers
- Opportunities for buy-and-build strategies in various sub-sectors
- FM companies tend to be asset and capex light
- Increasingly, long-term contracts are being structured with strong visibility of earnings

The European market is now home to a number of sizeable PE-backed FM companies such as Scandinavian cleaning services group Alliance+, Spanish security company Casesa, and UK-based vacant property specialist VPS Holdings.

Meanwhile, a number of PE-backed companies have made exits on the public markets in recent times such as: food and concession provider Aramark Corporation; French laundry services group Elis; Danish outsourcing group ISS; and Swedish plumbing and electrical systems group Bravida.

All were very active in the M&A market before their flotations. For instance: Bravida expanded significantly by acquiring a number of smaller Scandinavian players including Halmesvaara Oy and the Peko Group in Finland, and Electi EL and Electi Service AB in Sweden. Elis made a number of overseas acquisitions including Atmosfera, Clara and Acqua, and took a majority stake in RLD.

Recent deal highlights

- Bridgepoint Development Capital exited Penelope, a France-based provider of reception services for the events market. French PE firm LFPI has taken a majority stake in the business.
- PAI Partners acquired VPS Holdings, the European division of VPS Acquisitions, from TDR Capital. VPS is a leading European vacant property specialist providing security solutions.
- HIG Capital sold Europa Support Services, a leading provider of IFM services, to Bilfinger. During HIG's ownership, Europa made four bolt-on acquisitions.
- Investment holding company Kasigo Tiso Holdings (KTH) acquired a majority stake in the Servest Group, one of the largest FM companies in Africa. Servest also has a significant business in the UK where it has been increasing its IFM offering. Recent acquisitions in the UK include Facilities Services Group, Maxwell Steward, 7 Day Catering, and Stag Security.

Facilities Management, Private Equity Investments

Company	Country	Investor	Sector	Date
Premier Support Services	UK	Investec	Cleaning & security services and property management	2016
Sperber GmbH	Germany	Deutsche Private Equity	Technical building equipment services	2015
Waterfall	UK	LDC	Contract catering	2014
id verde	France & UK	Chequers Capital	Landscaping services	2014
Bellrock	UK	Lyceum Capital	Specialist FM and property management	2013
Lück Holding GmbH	Germany	Hannover Finanz	Technical building equipment services	2012
Segur Ibérica	Spain	Corpfin Capital & MCH Private Equity	Security services	2011
Casesa	Spain	Baring Private Equity	Security services	2010

Conclusion

As the global FM market has rapidly matured, so leading players have been busy enlarging their portfolio of services and becoming strategic rather than just service providers to their clients.

However, while growth in commodity markets has remained somewhat subdued in recent times, more niche value-added platforms can provide strong returns, and investor appetite for tech-enabled FM companies delivering high margin services remains strong.

Against this backdrop, we fully expect M&A activity to remain particularly strong in these more specialised markets throughout the rest of 2016.

Deal highlights

Some of our business services deals

Evander

Provider of 24/7 emergency response and repair for locks and glazing

Clearwater International advised Evander's shareholders, LDC and Bridgepoint Development Capital on the sale to vacant property services specialist VPS

Seguridad LPM SL

Spanish security systems and services company

Clearwater International advised the company on raising funding to buy two companies dedicated to alarm systems

Waterfall Services

Contract catering company focussing on the education, care and welfare sectors

Clearwater International advised the shareholders of Waterfall on the secondary buyout by LDC

Floor Cleaning Machines

Leading technical maintenance business within the UK retail floor cleaning market

Clearwater International advised the shareholders of Floor Cleaning Machines on its cross-border sale to Nilfisk

Kafevend Holdings

Fast-growing workplace vending suppliers

Clearwater International advised on the cross-border sale of the company to Eden Springs

SitexOrbis

Specialists in securing, maintaining and managing properties

Clearwater International advised the company's shareholders on the management buyout

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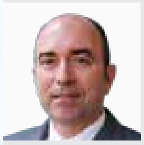

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