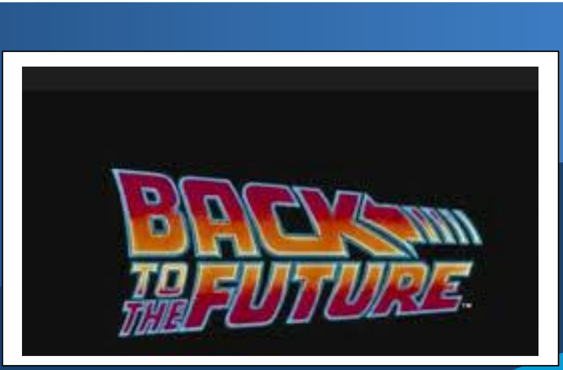

BACK TO THE FUTURE- “A Case Study”

I read recently the sad news of the passing of Sir Joe Dwyer, the ex-Chief Executive of Wimpey Plc, and his obituary relating his 44 years with the firm, joining as I did myself as a young engineer. His most notable contribution was recorded as his role in repositioning Wimpey as the UK’s largest pure housebuilder by swapping its contracting and minerals divisions for Tarmac’s housing division in 1995 in a combined £700m valued deal. He had become convinced by a company review highlighting that construction had proved a high-risk business offering low returns and considerable pain. The decision has been vindicated with Wimpey’s profits being recorded as having grown subsequently from £15m to £451m, according to The Times.

As head of the Corporate Development Unit for Wimpey Construction at the time I had been instructed to seek an exit strategy. I had in fact recommended a Tarmac-Wimpey Plc Group merger as the preferred strategy and the Asset Swap as an alternative, mindful that Group mergers involve substantial surgery at the executive level of combined overheads. I highlighted the benefit of a large well capitalized diversified and integrated merged Group being better able to weather inevitable industry cycles. But subsequent to the Asset Swap I was mindful that Wimpey would have negotiated the better deal, and aware that Neville Simms, the Tarmac Chief Executive, my previous boss and known advocate of contracting, would recommend the proposal to his Board, subject to due diligence.

While Tarmac had retained an integrated aggregate and contracting national business, city analysts were quick to force management’s hand to realize breakup values via demergers of undervalued combined diverse business operations. In July 1999 Carillion was created as a cash-rich contractor and facilities manager following the demerger and separate stock exchange listing. With a change of CEO, it went onto acquire many competitors and related businesses during the next decade until concerns about its growing debt situation were raised in 2015.

As Construction Groups divorced themselves from their asset-rich higher margin housing and minerals businesses, they became thinly capitalized contractors building up debt and goodwill by acquiring other lowly capitalized businesses as a route to their growth. This made them even more vulnerable to industry downturns. In 2016 I compiled a 360-page industry study, reporting companies’ statuses and recommending mergers of major contractors emulating the mainland European model of formation of mega-contractors, with the financial and human resources to survive. Company CEOs ignored the warnings as they focused on survival and in some cases misrepresentation of their financial positions.

In early 2018 Carillion became officially “the largest ever trading liquidation in the UK”. And by May 2018 a Parliamentary Inquiry Report stated that Carillion’s collapse was “a story of recklessness, hubris and greed with a business model being a relentless dash for cash, driven by acquisitions, rising debt, expansion into new markets and exploitation of suppliers. Coupled with this flawed business model, misrepresentation of the financial realities of a contracting business is difficult for an auditor to detect due to the large amount of work-in-progress and subjective valuation of partly completed contracts by project management.

Nevertheless, accountants and lawyers managing Carillion's liquidation were set to earn £70m in fees. Frank Field and Rachel Reeves co-chair of the Parliamentary Select Committee, with whom I was sharing information and opinion, concluded: "The dice are loaded in the Big Four's favour. They make a killing in fees advising struggling companies how to turn them around and then they pocket millions tidying up when the advice fails."

I had met with Carillion's CEO on several occasions before the imminent demise of the company, campaigning for the merger of the business with a cash-strong partner. By the end of 2017 I was recommending the company's advisers Ernst & Young to take seriously an expression of interest I had received from a Kuwait based conglomerate to acquire Carillion Group as a going concern and recapitalize it. I was advised that the company's corporate advisers, Lazards, favoured a strategy of disposals of business units. Soon after it became too late in the day for a defensive mega-merger.

The writing had been on the wall for some time prior. Before the company had issued a profit warning, the hedge funds were quietly assessing the signs of strain: disproportionate growth in trade receivables; poor cashflow performance; funding of dividends from disposal proceeds; high debt levels and pension fund deficits; and aggressive payment terms with suppliers.

During 2021, following the liquidation and administration of many other ailing contractors in 2018-2020, and as Managing Partner of Think Big Partnership, I once again began shouting from the roof-tops for companies to consider mergers as a strategy for survival. By November 2021 it had become evident that the industry needs new vision, leadership and substantial investment to bring about the industry consolidation to deliver well-capitalized construction groups capable of competing with European competitors on mega projects of the future.

Sir Neville Simms Foreword to the 2016 Think Big Partnership Industry Report stated, "British contractors are in danger of missing out on major international projects in the future, if they lack the financial muscle and diversity of say a £15bn-a-year contractor to handle the more complex projects. On the premise that further consolidation in the industry must and will take place, policies and strategies that lead to increased market share, more innovation, improving profitability and more certain returns to shareholders, should lead us to a construction sector that in the future is both financially and operationally stronger."

Now is the time to act, not talk, and the eventual model companies of the future may well mirror those well-diversified construction groups created by M&A in the UK in the 1980s. But Global capital and Foreign-led acquisitions may prove to be the catalyst this time around.

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