

UK CONSTRUCTION CONSOLIDATION 2017-2022

Corporate Strategies
and
M&A Opportunities

PRESENTATION



www.thinkbigpartnership.com



Greg Malpass

January 2017

**Power Point
Presentation**

Summary Report

What's the Framework for Change?

(Review-Innovate-Lead)



What is needed first?

(Industry Consolidation)



Sir Neville Simms FREng

“ Industry Consolidation must and will take place....

and company strategies that lead to increased market share, more innovation, improved profitability and more certain returns to shareholders should lead to a sector financially and operationally stronger.”



Which strategies will not achieve this?

(Retrenchment)



Leo Quinn

“Over the next 24 months I am confident we can reach industry standard margins and then build on the foundations.”

“Balfour Beatty needs to proactively get successfully acquired or merged, asap. That way it can easily achieve synergistic savings, and provide a compelling investment case for shareholders regarding the future direction and success of the company. While it is focusing on retrenchment and consolidation in its core contracting businesses, it does not have the luxury to do what it needs to do for the longer term, which is to put in place a strategy, and the financing, for future diversification outside contracting.”



The Lost Opportunity to start the Process?

(Carillion- Balfour Beatty Merger Opportunity 2014)

The Battle of The Hard Hats (2014)



Source: Evening Standard

“It is a fact that it was Balfour’s board, rather than its shareholders, who decided the fate of the merger.....

With the change in leadership at Balfour Beatty, maybe it’s time to re-open positive dialogue.”



What's Carillion's position now?

(Weaker as an Acquirer, strong as a Merger Partner)



Richard Howson



"Fortune favours the Brave."

Carillion's short term problems revolve around its pension Deficit and Debt levels, and its deteriorated Share Price, not helped by Short-Sellers.



Why are UK Companies outranked in Europe?

(Only the UK House Builders rank in Top 10 by Market Capitalisation)

Top 20 By Market Capitalisation

Rank	Company	COUNTRY	Market Capitalisation (€ m) 2015	Market Capitalisation (€ m) 2014	Variation 2015 vs 2014	Ranking change on 2014
1	VINCI SA	FRANCE	34,801	26,851	30%	-
2	FERROVIAL SA	SPAIN	15,270	12,029	27%	-
3	BOUYGUES SA	FRANCE	12,613	10,070	25%	-
4	TAYLOR WIMPEY PLC	UNITED KINGDOM	8,974	5,756	56%	↑ 5
5	BARRATT DEVELOPMENTS PLC	UNITED KINGDOM	8,625	5,998	44%	↑ 3
6	ACTIV. DE CONSTR. Y SERV. SA (ACS)	SPAIN	8,501	9,116	(7%)	↓ 2
7	PERSIMMON PLC	UNITED KINGDOM	8,427	6,198	36%	-
8	SKANSKA AB	SWEDEN	7,373	7,505	(2%)	↓ 3
9	ENKA INSAAT VE SANAYI AS	TURKEY	5,704	6,712	(15%)	↓ 3
10	EIFFAGE SA	FRANCE	5,493	3,886	41%	-
11	ACCIONA SA	SPAIN	4,528	3,218	41%	-
12	BELLWAY PLC	UNITED KINGDOM	4,195	3,043	38%	↑ 1
13	NCC AB	SWEDEN	3,088	2,845	9%	↑ 1
14	CFE	BELGIUM	2,762	2,152	28%	↑ 1
15	BALFOUR BEATTY PLC	UNITED KINGDOM	2,528	1,877	35%	↑ 4
16	STRABAG SE	AUSTRIA	2,419	2,072	17%	↑ 1
17	PEAB AB	SWEDEN	2,082	1,732	20%	↑ 5
18	JM AB	SWEDEN	2,024	2,043	(1%)	-
19	GALLIFORD TRY PLC	UNITED KINGDOM	2,015	1,361	48%	↑ 6
20	SALINI IMPREGILO SPA	ITALY	1,980	1,501	32%	↑ 3

Source: Bloomberg



Why are Global E&C Groups in a Different League?

(No UK Companies rank in Top 25)

ENR Ranking		
Company	Country	Ranking 2015 vs 2014
China Railway Group Limited	China	↑ 2
China State Construction Engineering Corporation	China	↓ (1)
China Railway Construction Corporation Limited	China	↓ (1)
China Communications Construction Company Limited	China	=
Vinci SA (**)	France	=
Activ. de Constr. y Serv. SA (ACS) (**)	Spain	=
Power Construction Corporation of China (*)	China	↑ 7
Bouygues SA (**)	France	=
Hochtief Ag (***)	Germany	↓ (2)
Metallurgical Corporation of China Limited	China	=
Bechtel Corporation (*)	Usa	↓ (2)
Shanghai Construction Group (*)	China	↓ (1)
Cimic Group (***)	Australia	=
Skanska Ab (**)	Sweden	↑ 1
Fluor Corporation	Usa	↓ (3)
Strabag Se (**)	Austria	=
Hyundai Engineering & Construction Corporation	S. Korea	↑ 3
Obayashi Corporation	Japan	=
Eiffage (**)	France	↓ (2)
Technip (****)	France	↑ 5
Samsung C&T Corporation	S. Korea	↑ 2
Construtora Norberto Odebrecht	Brazil	↓ (3)
Saipem (****)	Italy	N/A
Kajima Corporation	Japan	↓ (2)
Shimizu Corporation	Japan	↓ (4)

Source: Deloitte

Who are the Top 15 UK Contractors/ Housebuilders?

(The Top 5 command more than 50% of Top 15 Turnover)

Rank 2014	Rank 2015	Construction Company UK (including Housing)	2014 T/O (£m)	Change %	2015 PBT (£m)	Year End	Contracting	Housing	Property	Services	Other
1	1	Balfour Beatty Plc	8,793		-304	Dec-14	6,597			1,273	570
2	2	Carillion Plc	4,072	-0.2	173	Dec-14	1,600			2,412	162
3	3	Laing O'Rourke	3,574	0.2	52	Mar-14	3,574				
4	6	Interserve Plc	3,305	28.0	62	Dec-14	1,176			1,913	215
5	5	Barratt Dev's	3,157	21.1	391	Oct-14		3,142	14		
6	4	Kier Group PLC	2,985	11.8	73	Jul-14	1,597		284	1,104	
7	7	Taylor Wimpey	2,686	17.0	450	Mar-14		2,686			
8	10	Persimmon	2,574	23.2	467	Dec-14		2,573			
9	11	Amey Group	2,416	21.1	106.7	Dec-14	1,180			639	
10	8	MITIE	2,266	5.8	41.5	Mar-15			273	1,901	103
11	9	Morgan Sindall	2,220	6.0	22.8	Dec-14	1,172	423	130.3	507	
12	13	Berkeley Group	2,120	30.8	539.7	Apr-15		2,120			
13	12	Galliford Try	1,768	10.2	95.2	Jun-14	833	1,002			15
14	14	BAM UK	1,600	0.0	7.2	Dec-13	1,600				
15	16	Bouygues UK	1,600	13.2	28.3	Dec-14	1,600				

Source: Building.co.uk

Time for Change?

Industry Structure



"I'm a small builder"



MARKET ANALYSIS



Focus on Top 5 being formed from Mergers of Top 15



²Source: EY

- Balfour Beatty
- Carillion
- Interserve
- Laing O'Rourke (Private Co)
- Kier Group
- Taylor Wimpey
- Morgan Sindall
- Vinci/Taylor Woodrow
- Amey Uk/ Ferrovial
- Galliford Try
- BAM
- Bouygues
- Skanska
- Costain
- Dragados

Top 5 Listed Companies

Balfour Beatty

 carillion

 Interserve

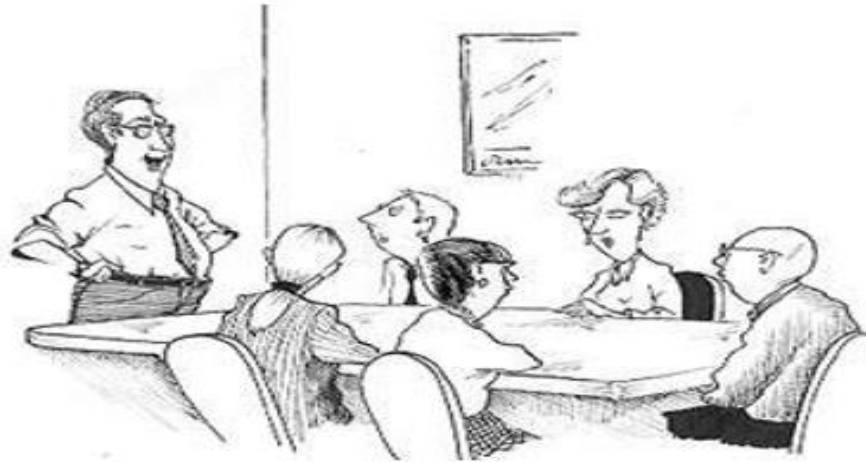
Taylor Wimpey

 **KIER**



Reviewing Performance?

Performance Review



"I think we're in good enough shape to start making the same mistakes again."



MARKET ANALYSIS



How do they compare in Size & Performance?

(Top 5 Financial Performance Stats)

TOP 5 2015 COMPARISONS	2015 TURNOVER (bn)	2015 MARKET CAP (bn)	PBT (m)	NET DEBT (m)	PENSION DEFICIT (m)
BALFOUR BEATTY	8.444	1.915	-199	155	146
CARILLION	4.587	1.068	155	188	406
KIER	4.112	1.156	-18	153	123
INTERSERVE	3.629	0.656	115	322	-17
TAYLOR WIMPEY	2.723	5.011	604	-128	178





MARKET ANALYSIS



Company Analysis

www.thinkbigpartnership.com



"The company may not be a lead player in the UK, but has its niche market strengths and some pros when it comes to being a potential M&A target :

- ***no financial debt***
- ***management holds significant shares***
- ***no majority shareholder***
- ***constant and high ROE/ROE/ROIC***
- ***long established operating history***
- ***almost no pension liabilities***

It is recommended interested parties speak to the Company's founder and Chief Executive."

Kier



See page 10 for more

See page 14 for more

Property	Residential	Construction	Services
The Property division provides property development and structured project finance.	The Residential division, known as Kier Living, brings together all of Kier's house building operations from contracting and mixed tenure housing to private sector housing.	The Construction division comprises regional building, major projects, infrastructure and international operations.	The Services division comprises highways maintenance, utilities, facilities management, housing maintenance, environmental and fleet & passenger services.



"In recent years, since Dodd's departure as CEO, Kier seem to have cast old MBO conservatism about Acquisitions to the wind."



MARKET ANALYSIS



Galliford Try



“Galliford is a strong Diversified Housing and Construction Group with a Market Capitalisation of £1.1bn, a Turnover of £2.5bn, PBT £135m and Net Assets of £600m. It will continue to enjoy a buoyant housing market, and may choose to grow by Merger with another complimentary Group”



Peter Truscott

Recent Share Price Movements



Costain



Andrew Wyllie



"Following a *Be Safe* Strategy will not save Costain from inevitability of being Acquired."



Interserve



Adrian Ringrose



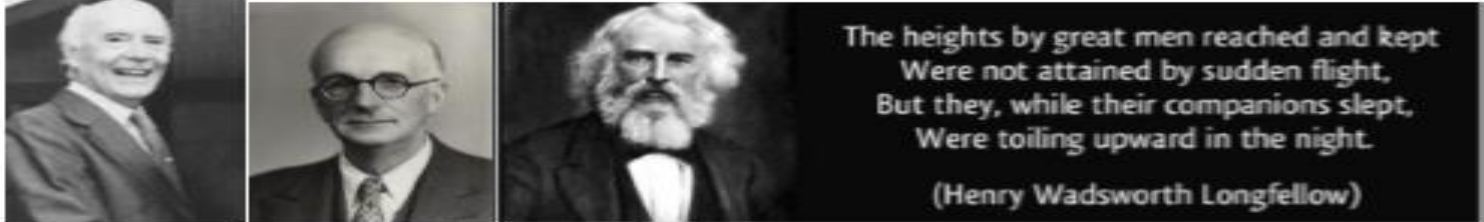
"Adrian Ringrose has built up a support services business from its roots as Tilbury Douglas. He has had his set-backs like the August 2006 announcement to the London Stock Exchange that accounting issues relating to the mis-statement of accounting balances had resulted in a £30m write-down, But the Group is strong and well diversified. With a Middle East presence as well, and a nominal Pension Deficit compared with its peers, Interserve is a good candidate for merger to form one of the top tier construction groups in the UK. Due to its low Market Capitalisation, it could otherwise become an acquisition target."



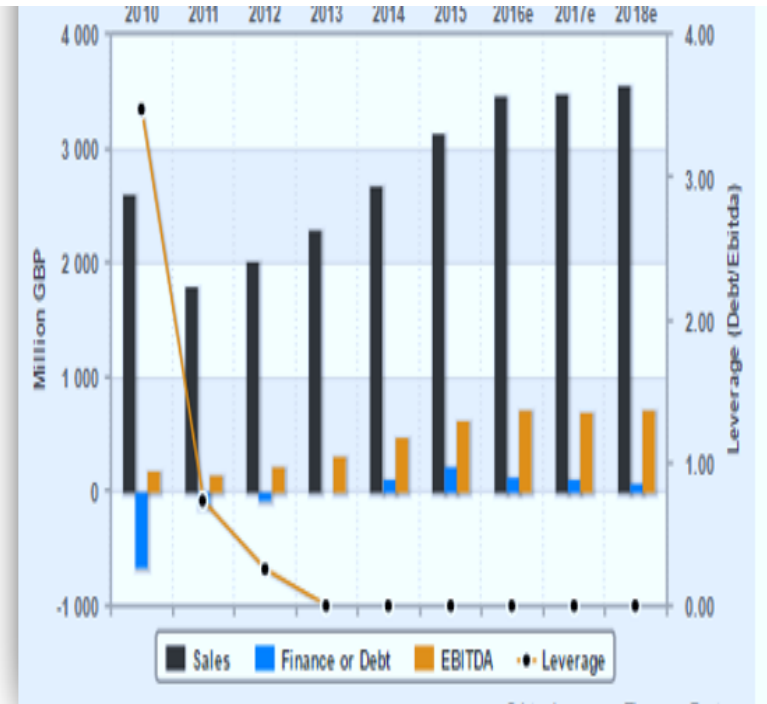
MARKET ANALYSIS



The Star Performer

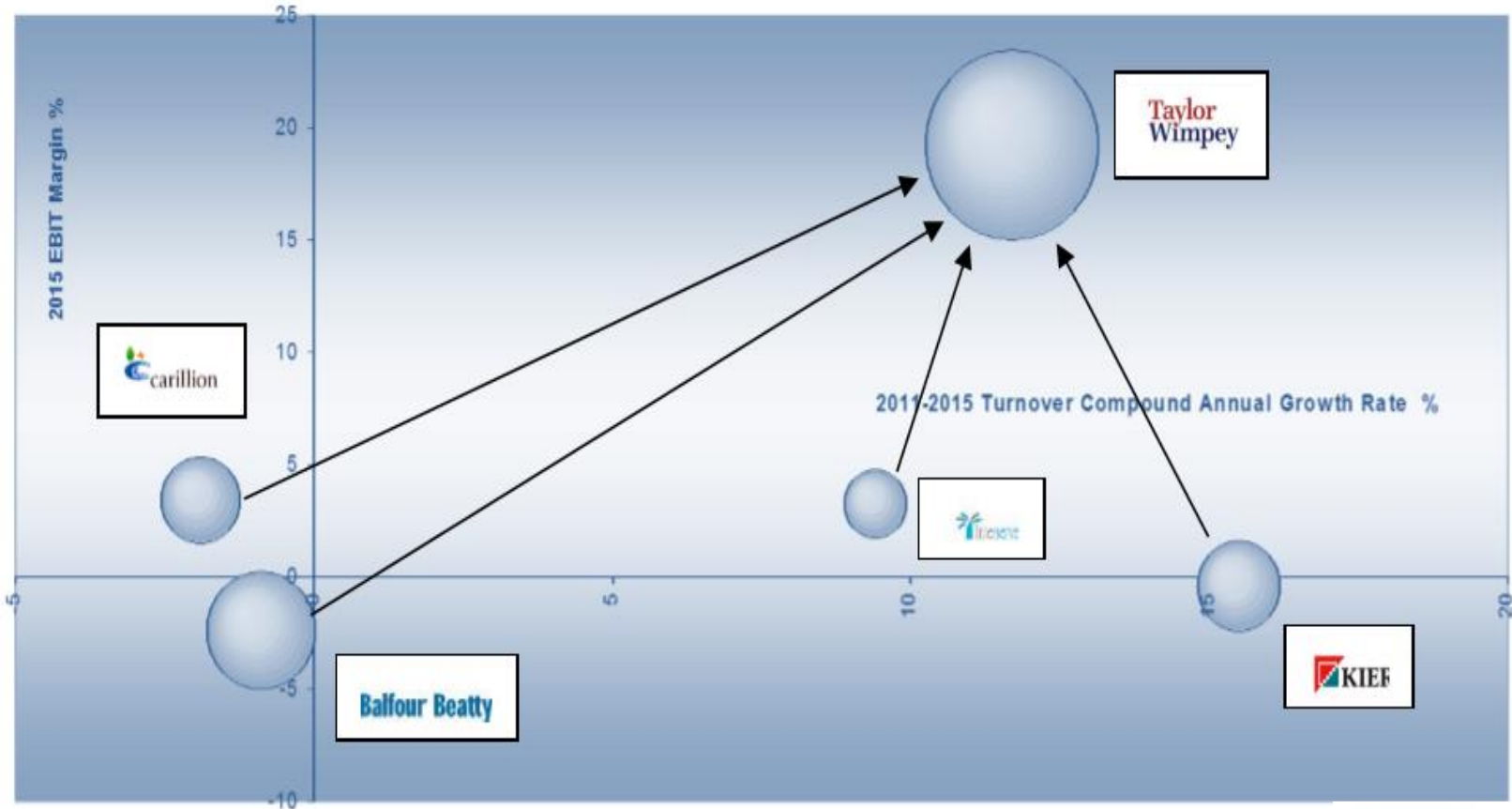


"Taylor Wimpey is a star performer among current UK Construction Groups, even though it cannot be described in any way as widely diversified. Strong Revenues, Profits, Order Book and a quality Land Bank have earned it a deserved c. £5bn Market Capitalisation. Quite a turnaround from the woes of the Post -Merger company debt Crisis and market downturn it faced in 2007. But the Group needs to look to its longer term future, and its new focus might well be on capitalising on its financial strength to diversify outside its total dependency on the UK Housing Market, despite its current buoyancy and outlook."



Taylor Wimpey sets the Benchmark

Industry Growth/Profitability Matrix (2016)



MARKET ANALYSIS



So What's the Right Strategy?

Strategy



“Ten minutes left- Let's do the strategy.”



MARKET ANALYSIS



Construction Outlook looks Favourable

(But there remain Barriers)



“The current economic fundamentals and committed major project pipeline, including significant opportunities in areas such as infrastructure and house building, should provide a backdrop in which the UK construction industry thrives. However, Industry structure and company-specific challenges remain a barrier to a more operationally and financially robust construction sector. The sector remains handicapped by risk across the contract life cycle, weak portfolio management, poor cash management, margin pressure and flawed structures and procedures.”





The Key Drivers For Consolidation?

- Globalisation - few, if any, construction companies with a truly global footprint
- Southeast Asia threat — buyers looking to invest in UK/EMEIA as an outlet for raw materials
- Major Projects - construction contracts increasing in size e.g., Crossrail, HS2, Hinkley, etc.
- ‘Corporatisation’ — economies of scale

ERNST & YOUNG VIEW ON CONSTRUCTION 2025- CONSOLIDATION AHEAD

To maximise shareholder value, management needs to make a clear assessment whether to focus on consolidation or being successfully acquired. Either way, there is a need for winning strategies that will enhance returns. *Ernst & Young (EY)* sets out its case in conclusions about four areas for focus and advice:

What can be learned from Company History?

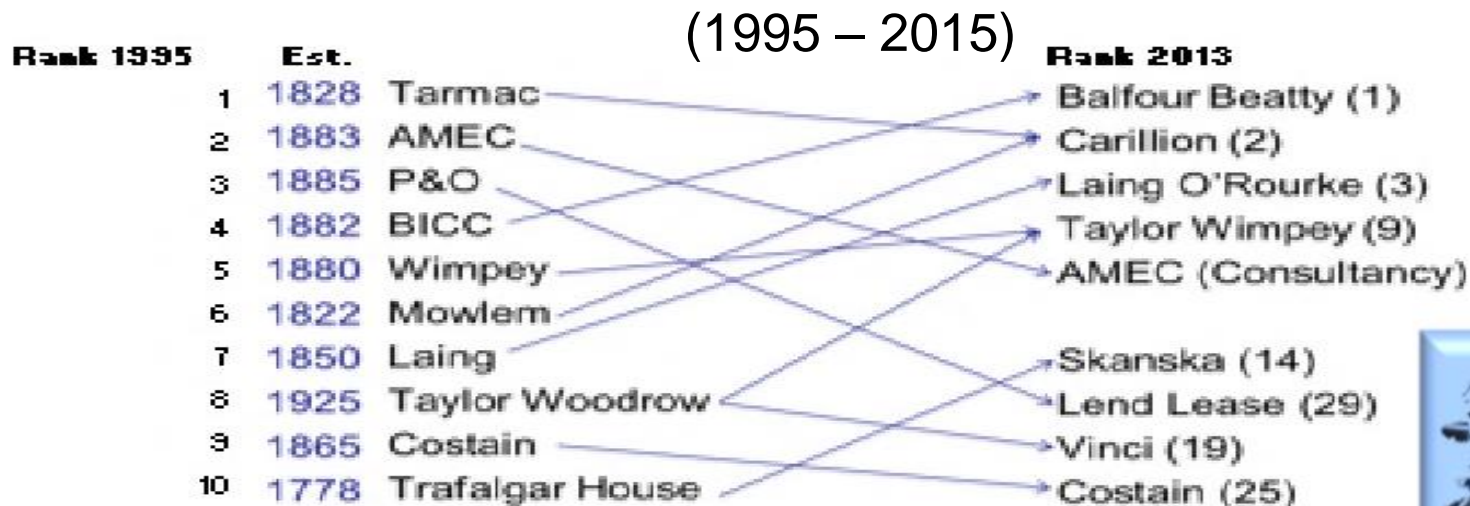
THE TOP UK CONSTRUCTION & HOUSING GROUPS IN 2015
ARE THE LEGACIES OF THE BREAK-UPS OF LARGE DIVERSIFIED
INTERNATIONAL CONSTRUCTION GROUPS IN THE 1980-1990s



Under changing Leadership & Strategies (1822 – 2015)

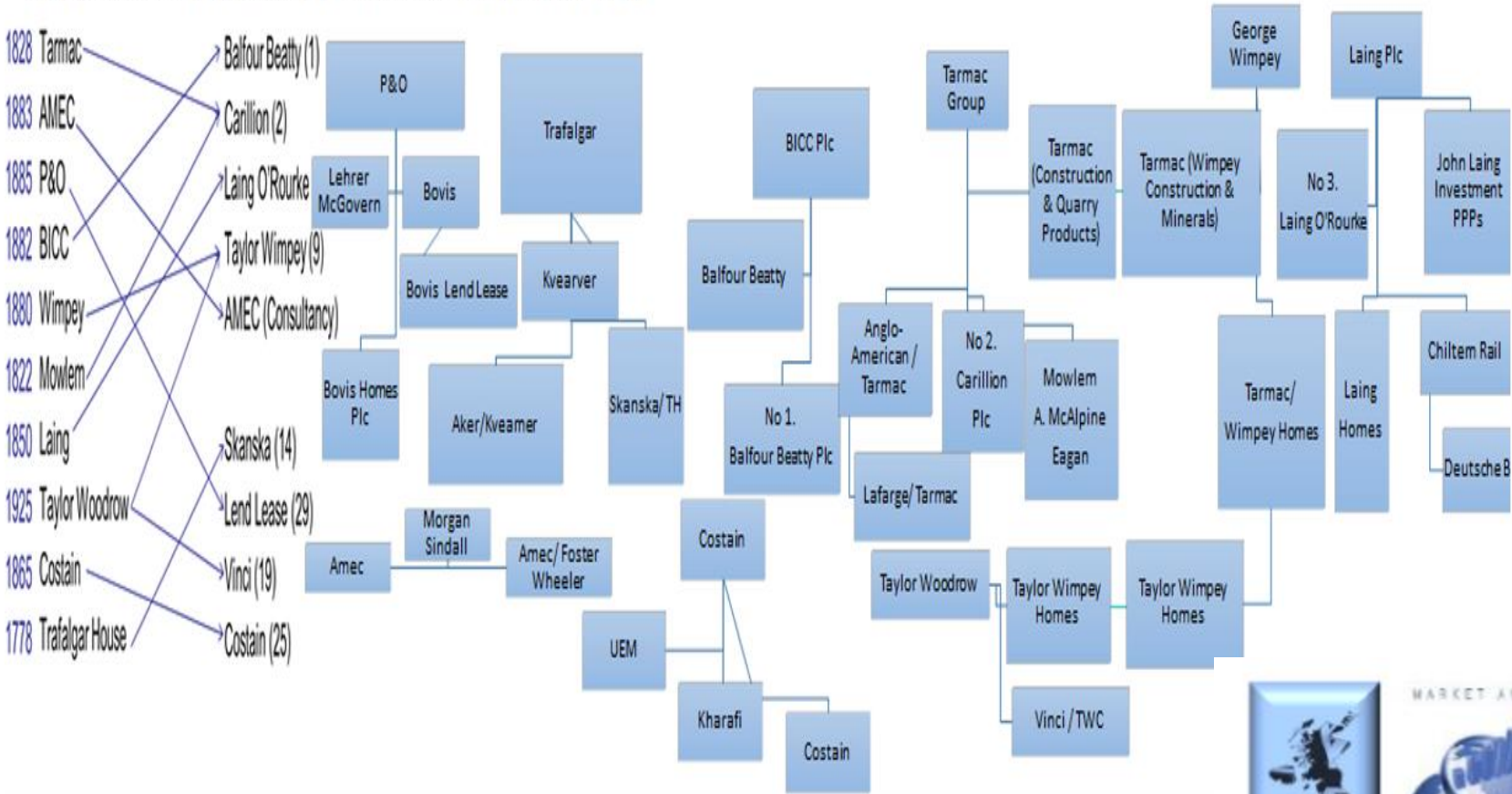


With resultant changes in Rankings



The Trail of Companies' M&A (1995-2015)

MAJOR MERGER & ACQUISITION TRAIL (UK CONSTRUCTION INDUSTRY 1995- 2015)



MARKET ANALYSIS

And some Recent E&C Acquisitions

Date	Acquirer	Target	Enterprise Value	EBITDA
03/29/16	 Stantec	 MWH	\$ 793	9.5x
03/23/16	 1347 CAPITAL	 LIMBACH	70	8.5
11/12/15	 salini Impregilo	 LANE	406	NA
10/14/15	 TETRA TECH	 coffey	126	8.2
10/03/15	 TRC	 WSP	130	8.8
08/25/15	 WSP	 MMM GROUP	310	8.9
08/14/15	 LLCP	 Trinity Consultants	375	12.0
07/01/15	 GENERAL ATLANTIC	 ENengineering	NA	11.0
09/03/14	 WSP	 PARSONS BRINCKERHOFF	1,243	8.8
08/07/14	 COMPASS	 CLEAN EARTH	243	8.3
07/31/14	 ARCADIS	 Hyder	451	12.9
07/13/14	 AECOM	 URS	5,584	7.3
06/23/14	 SNC-LAWALIN	 KIEWIT	1,695	13.7
03/12/14	 WSP	 FOCUS	329	8.3
01/13/14	 amec	 FW	2,816	9.6
09/08/13	 JACOBS	 SKM	1,100	7.2
07/30/12	 CBI	 Shaw	1,910	



So- To do nothing has never been a Strategy.

Change



**"What if we don't change at all....
And something magical just happens?".."**



MARKET ANALYSIS



And those who do nothing over time get Acquired

Acquire or be acquired



"This is our position"

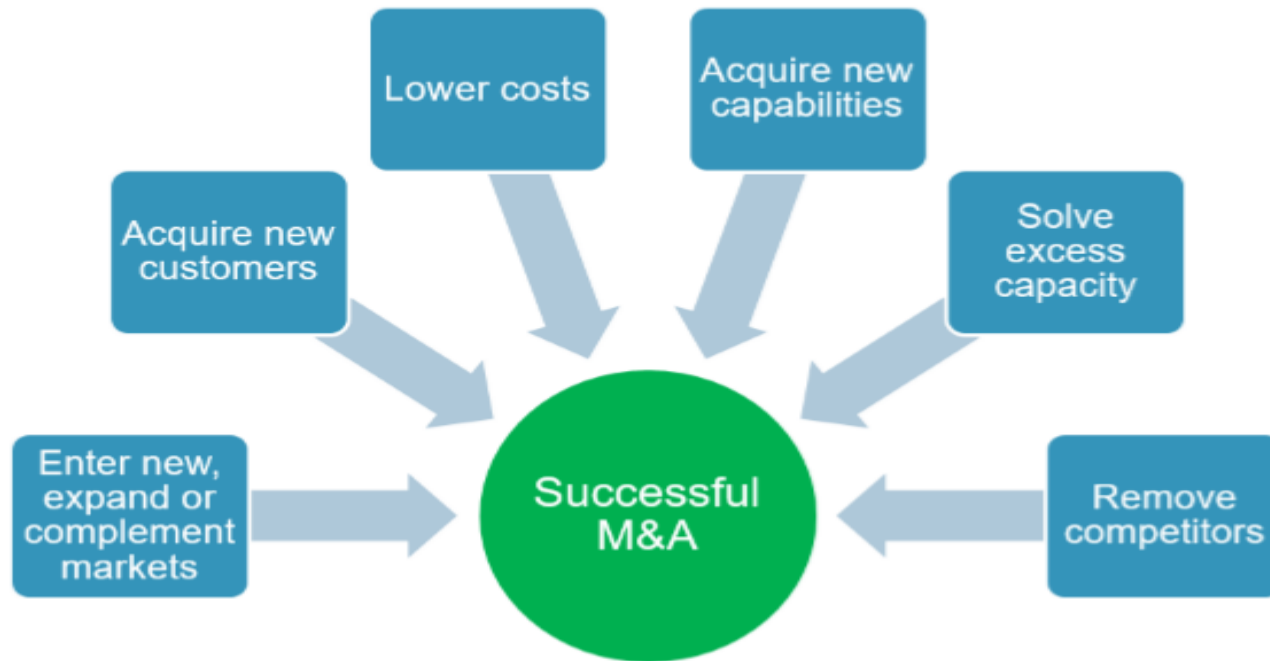


MARKET ANALYSIS



Need to understand what the M&A will provide

"Whether this acquisition can be deemed a success, time will only tell."



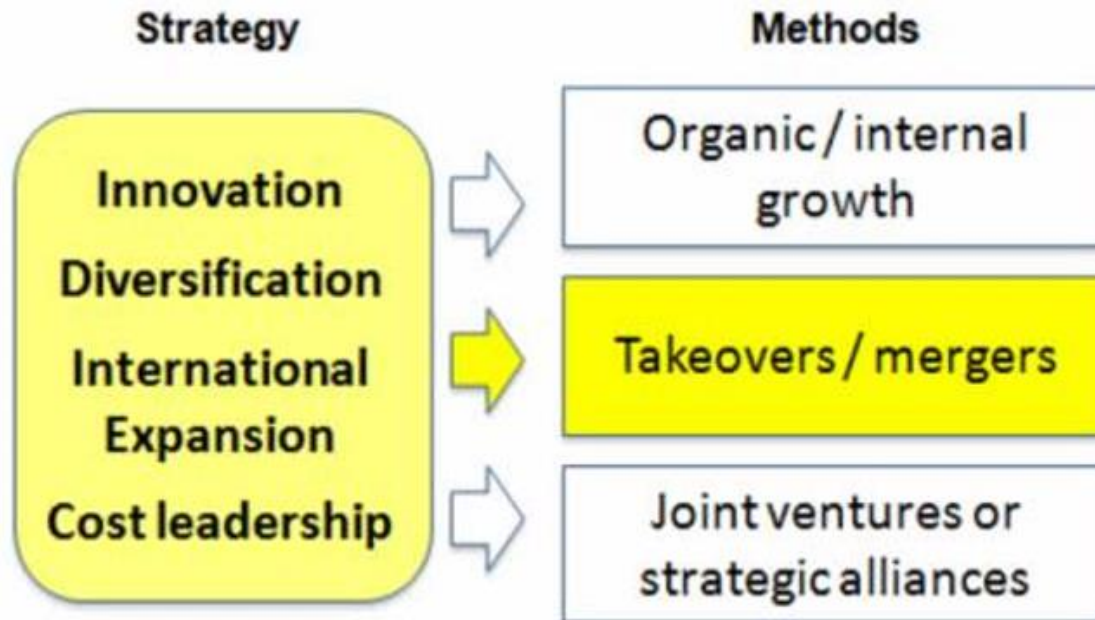
These are EY's Characteristics for a Major Group



MARKET ANALYSIS



The overall Strategy will only be delivered by M&A



Merger or Acquisition has to be decided up-front?

Post-Acquisition Integration



MARKET ANALYSIS



And consider who might align to form Groups?



Public Private Partnerships
 UK Export Finance
 Support Services & Facilities Management
 Investment, Mergers & Acquisitions

- Healthcare
- Energy
- Education
- Infrastructure
- Sanitation
- Defence & Security

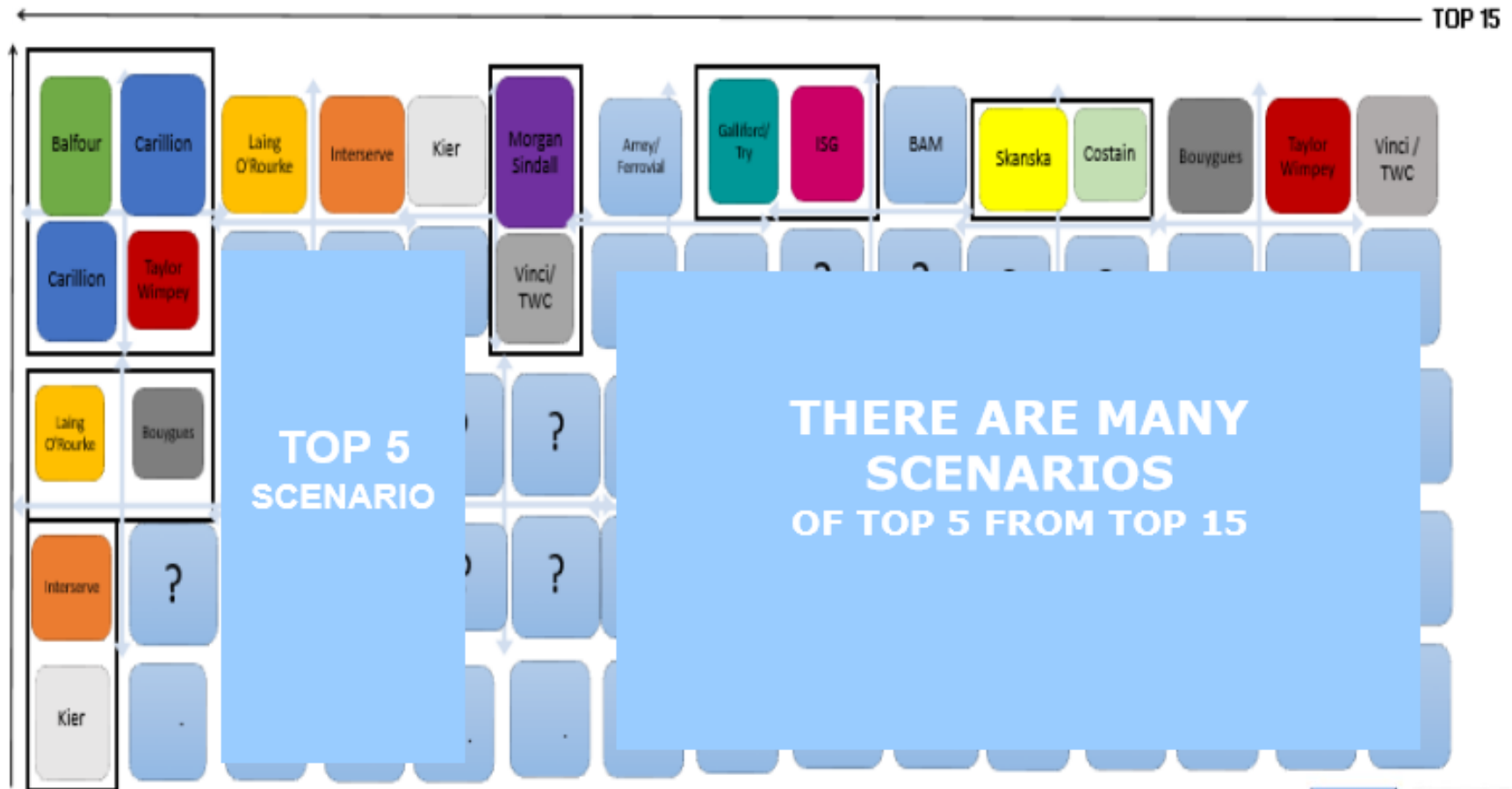


The "BIG" GROUP SHOULD BE DIVERSIFIED IN MARKETS & SECTORS & DISCIPLINES

11



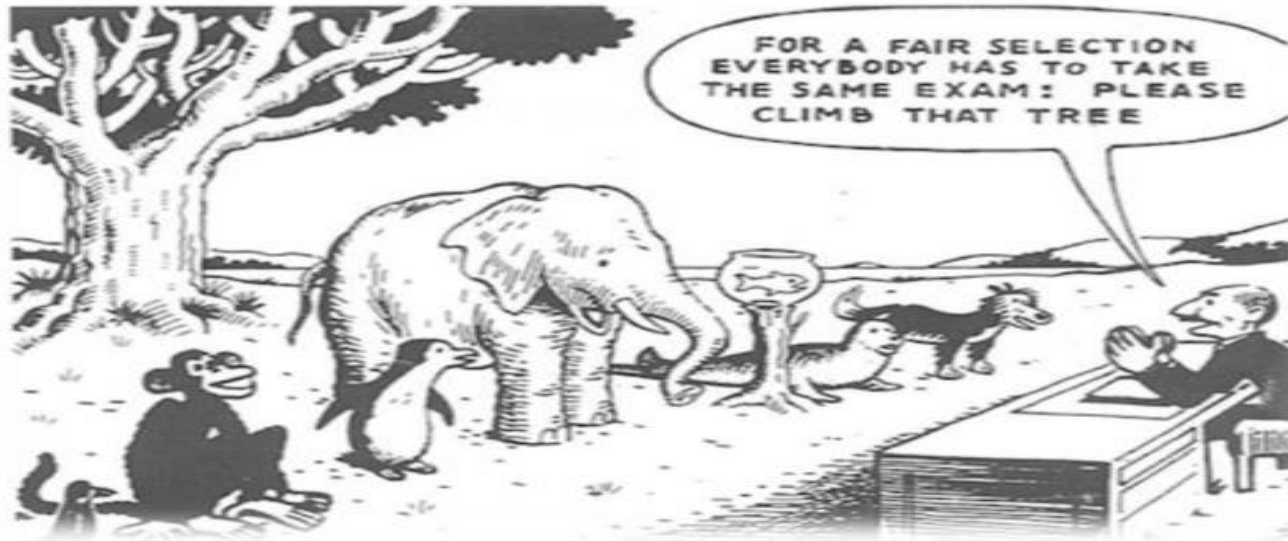
There are Multiple scenarios for Mergers



The Right M&A Selection is crucial

(Often there is only one obvious partner)

Acquisition Target



“Selection criteria”



MARKET ANALYSIS



What are the Competitor Strengths?

(Looking for strength in Combination)



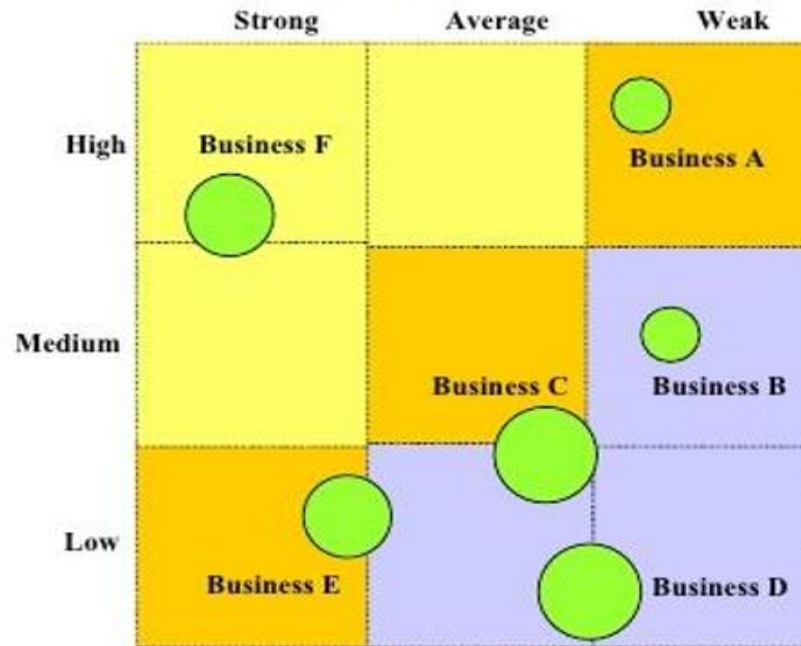
www.thinkbigpartnership.com

A -Costain's weak financial position has for a long time impaired its ability to capitalise on the full potential in its core markets. Target for Acquisition by Foreign Contractor with stronger Balance Sheet.

B- Morgan Sindall remains a small cap in terms of the Majors and its market positioning is average. Dull outlook without a growth strategy. Possible Acquisition Target.

**LONG-TERM
INDUSTRY
ATTRACTIVENESS**

COMPETITIVE STRENGTHS/BUSINESS POSITION



C- Laing O'Rourke retains good positions in UK Major Projects like Hinkley, but pulling out of successful Australian Business to lick wounds in Europe. A great success story, albeit a little tired. Time for new blood and shareholding?

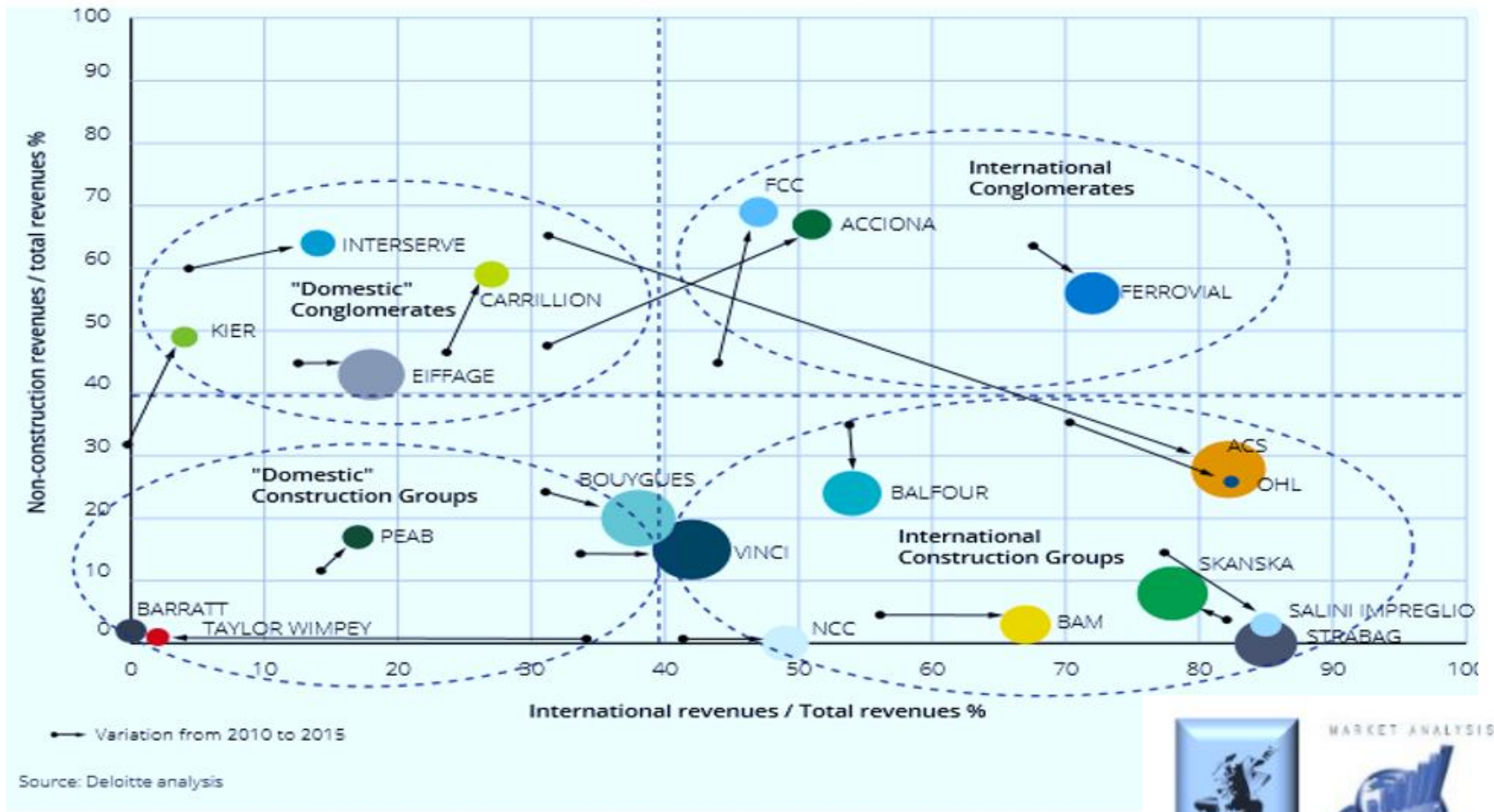
D- Balfour Beatty is plagued by its portfolio of loss making UK Projects and needs to seek overhead reduction through synergies as it trades out of its low margin UK contracting exposure.

E- Kier has strong market positions but its Infrastructure and Overseas operations are modest, and needs to look to long term attractiveness

F- Galliford remains in Construction, PPP and Housing and maintains a strong market capitalisation and could go far if strategic in its next stages of growth.

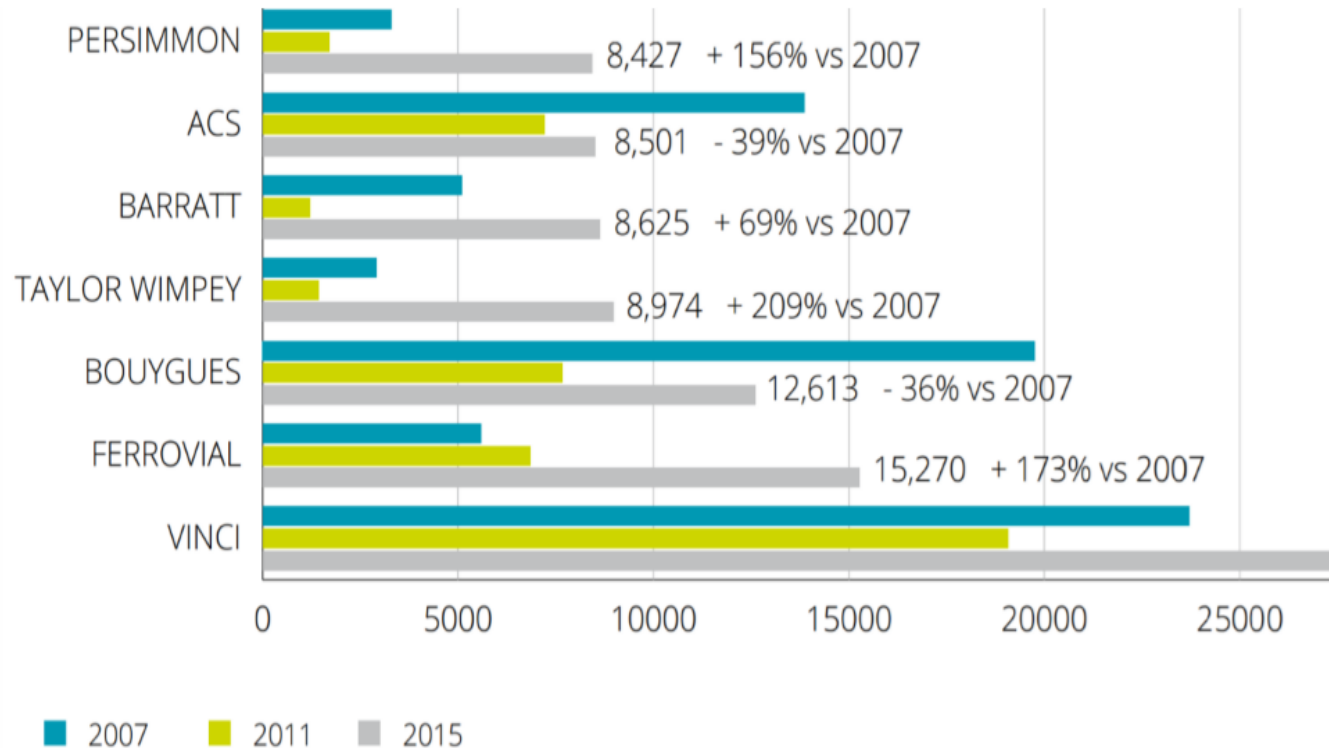
- High priority for investment
- Medium priority for investment
- Low priority for investment

Note the European Trends in Diversification (Those who have become International Conglomerates lead)



And where the European Market Strength is

(In terms of Market Capitalisation 2015 v 2007)

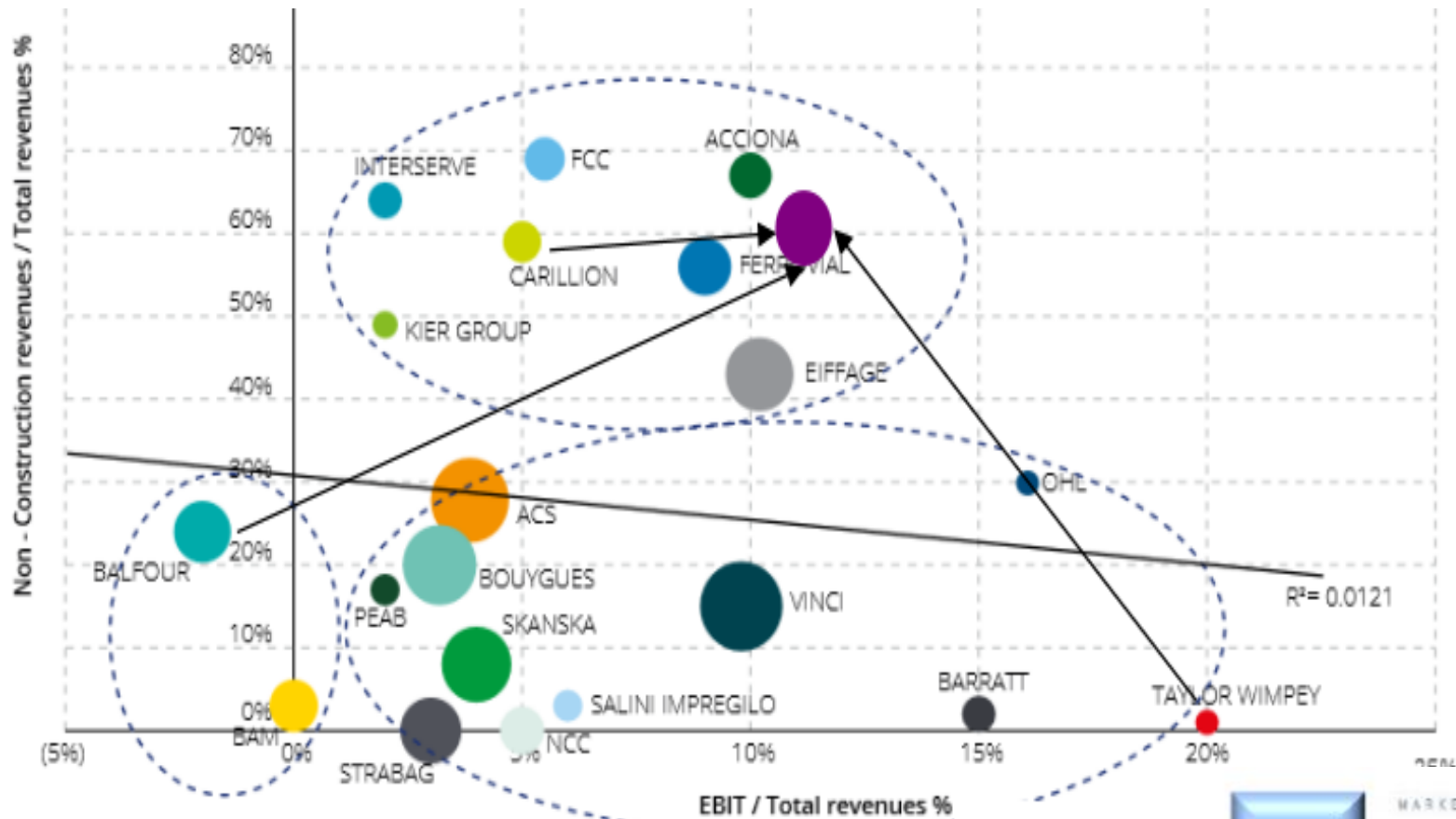


“The greatest strides in increasing Market Capitalisation dominance have been made by Vinci, Ferrovial, Bouygues and Taylor Wimpey, the latter which increased its value by more than 200%.”

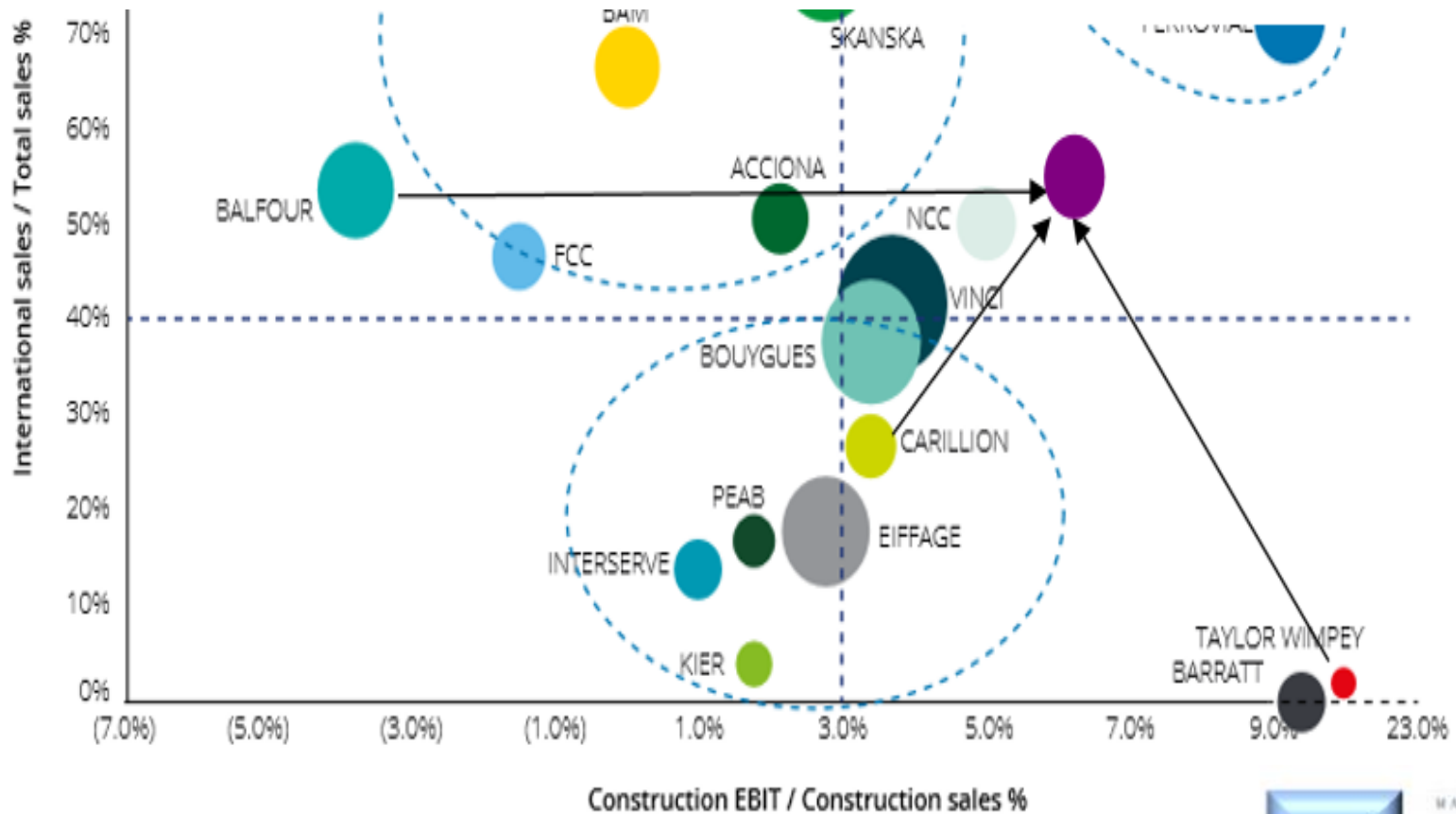
Taylor Wimpey also ranks most favourably, compared with its European peers based on its low gearing, indicating it has great scope to finance growth.”



Set a Target for future Diversity and Profitability (Using Competitor Analysis as a Template)



Consider Internationalisation v Profitability



MARKET ANALYSIS



What Innovation is required to achieve the Goal?

Innovation & Investment



"This really is an innovative approach, but I'm afraid we can't consider it. It's never been done before."



MARKET ANALYSIS



Ferrovial - a Case Study of Achievement

(From Domestic Contractor to Global End-to-end Infrastructure Company)

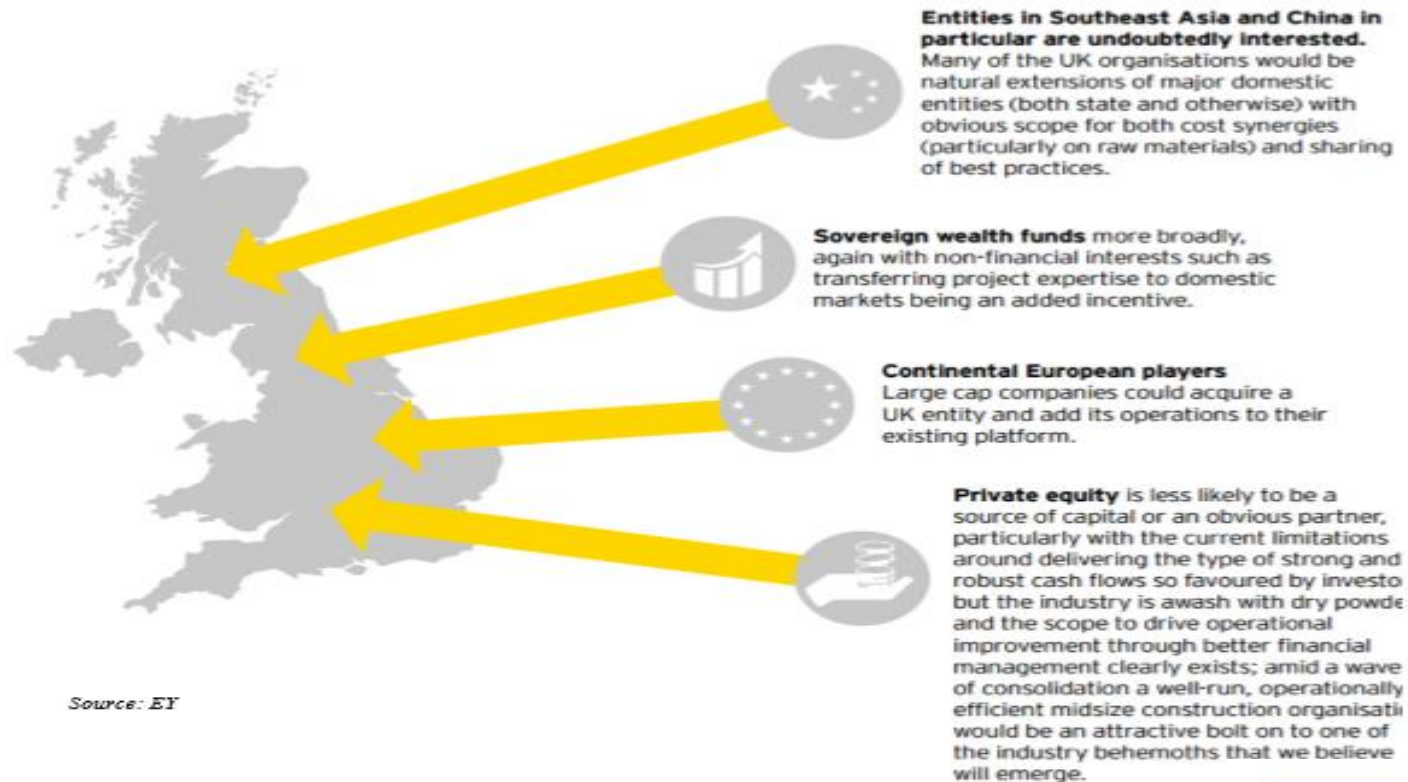
End-to-end infrastructure company: DFBOM



Ferrovial



What are the Possible Sources of External Capital (Possible Threats and Opportunities)



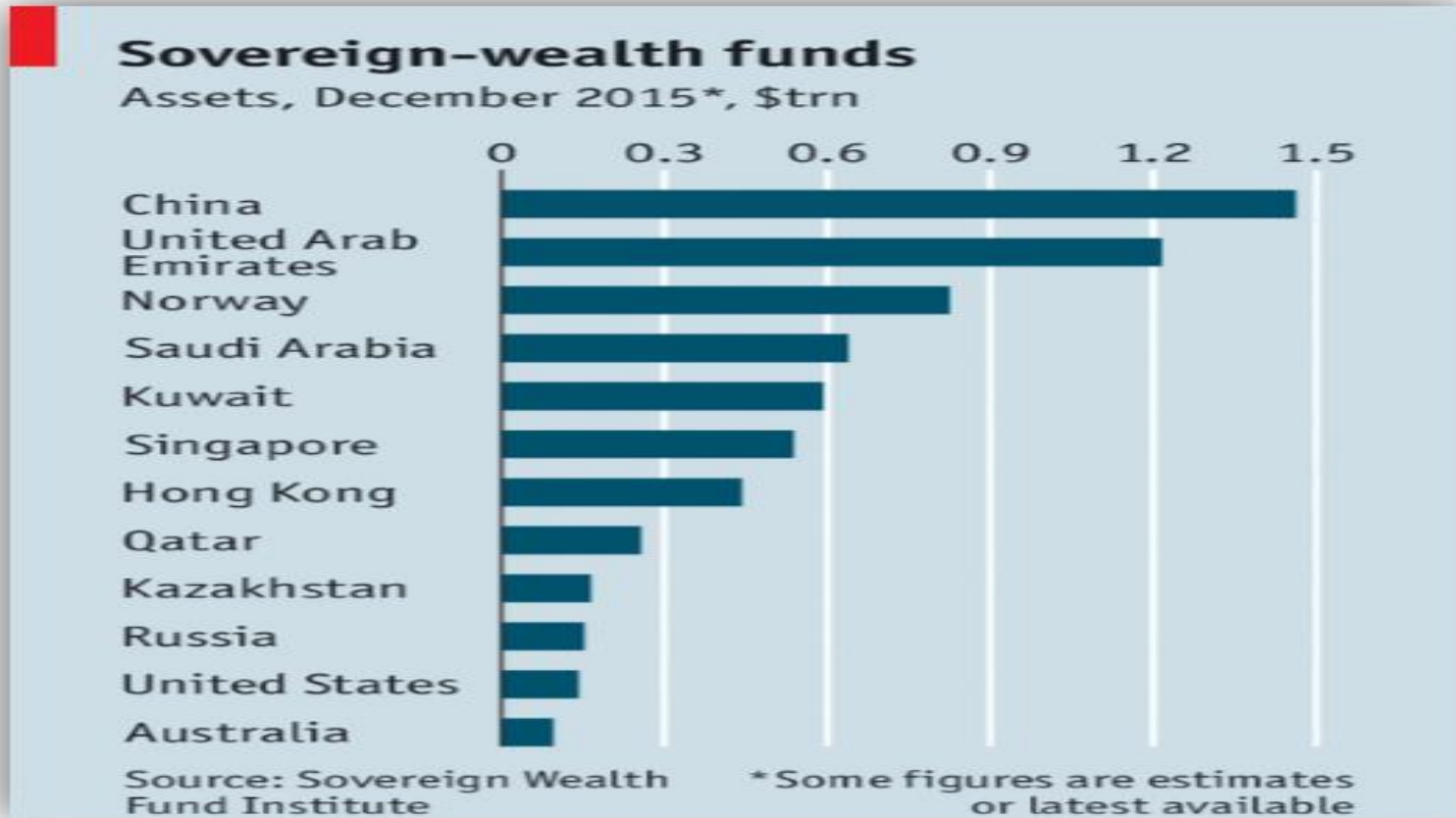
Source: EY



MARKET ANALYSIS



Sovereign Wealth Funds



MARKET ANALYSIS



Private Equity Firms

Rank	Name of the firm	Capital Raised as of Apr 2011 (billions of USD)
1	TPG Capital	\$50.55
2	Goldman Sachs Capital Partners	\$47.22
3	The Carlyle Group	\$40.54
4	Kohlberg Kravis Roberts	\$40.21
5	The Blackstone Group	\$36.42
6	Apollo Management	\$36.42
7	Bain Capital	\$33.81
8	CVC Capital Partners	\$29.40
9	First Reserve Corporation	\$25.07
10	Hellman & Friedman	\$19.06
11	Apax Partners	\$17.20
12	General Atlantic	\$16.60
13	Warburg Pincus	\$15.00
14	Cerberus Capital Management	\$14.90
15	Advent International	\$14.52
16	Permira	\$13.67
17	Oaktree Capital Management	\$13.05
18	Terra Firma Capital Partners	\$12.25
19	Providence Equity Partners	\$12.10
20	Clayton, Dubilier & Rice	\$11.40



MARKET ANALYSIS

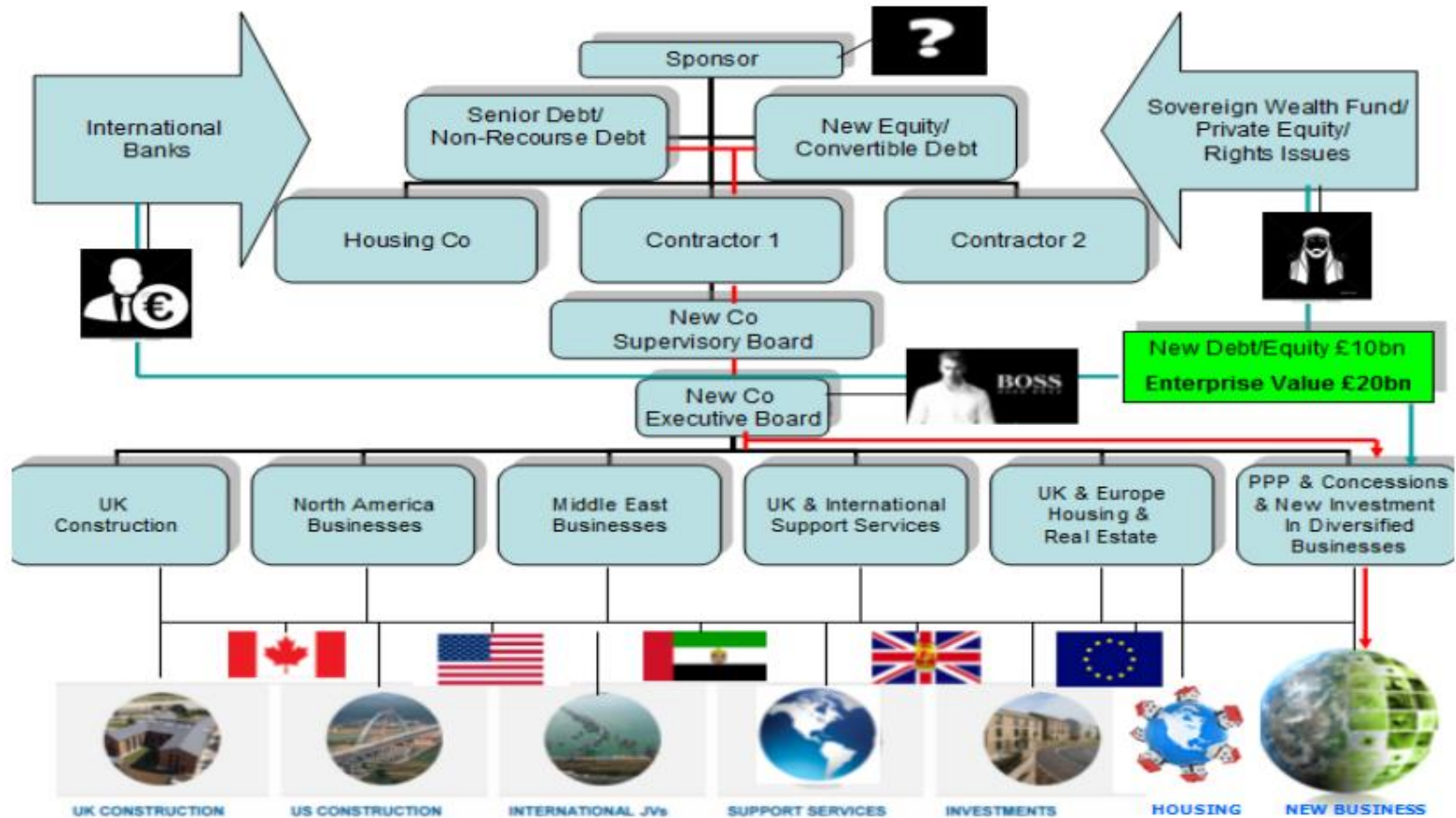


A scenario with Middle East Focus



A scenario of Major M&A led Growth

(Consolidation via Merger & Diversification via Investment)



MARKET ANALYSIS



The Key Message

"The message to UK Groups is one that I trust resonates throughout this voluminous Report:

- Consolidation is necessary and best achieved through Domestic Mergers between the strongest Groups which will benefit from Synergies and strengthened Balance Sheets*
- Post Consolidation, the emphasis should shift to new Diversification in terms of Non-Construction Activity and Geographical expansion.*

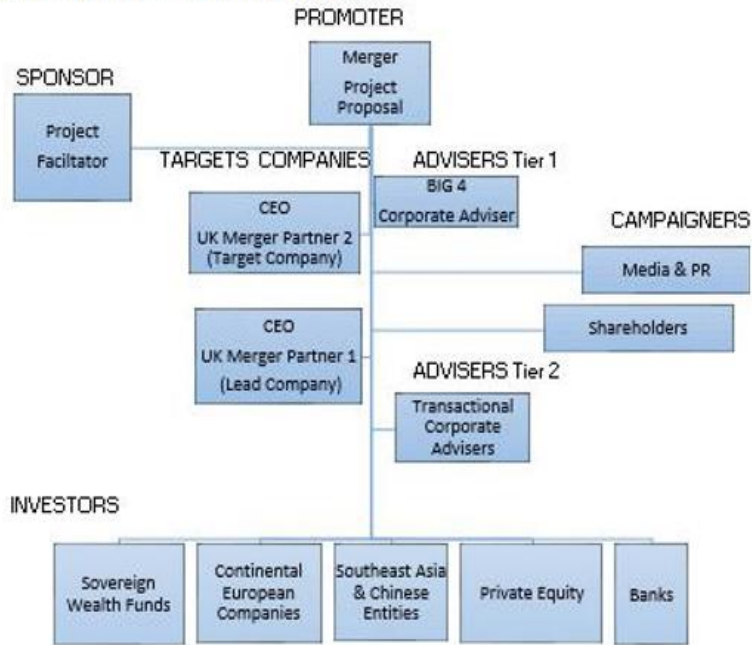
Those Groups with the strongest current market positions in their core markets, and low levels of debt- are best placed to achieve these two steps of Consolidation and subsequent Diversification successfully."



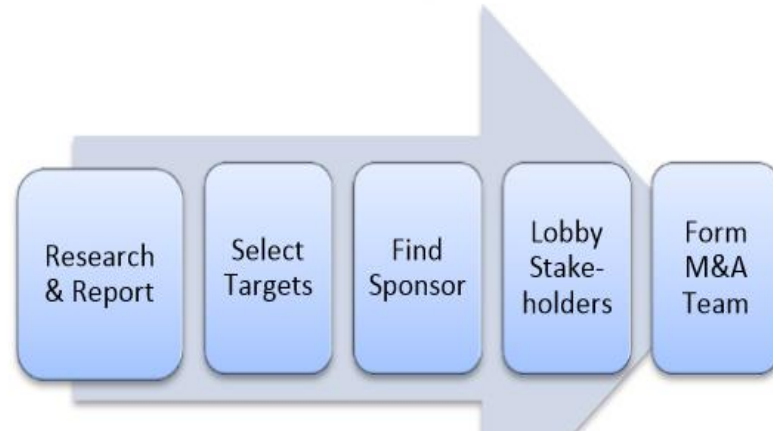
Putting Merger Strategy into Action?

(What are the Steps)

M&A STRATEGY - STAKEHOLDERS



M&A STRATEGY - PROCESS CHART



Gather Inputs

- From all Stakeholders
- Customer analysis
- Competitor analysis
- Industry analysis
- Environmental
- Company performance
- Company

SWOT Analysis

- External Analysis
 - Opportunities
 - Threats
- Internal Analysis
 - Strengths
 - Weaknesses
- Strategic Questions
- Strategic Issues

Review Inputs

- All Stakeholders
- Review Inputs
- Review SWOT Analysis
- Define 3-4 key statements

Strategic Matrix

- All Stakeholders
- Define Strategies to address SWOT combinations:
 - Opportunities vs Strengths
 - Opportunities vs Weaknesses
 - Threats vs Strengths
 - Threats vs Weaknesses

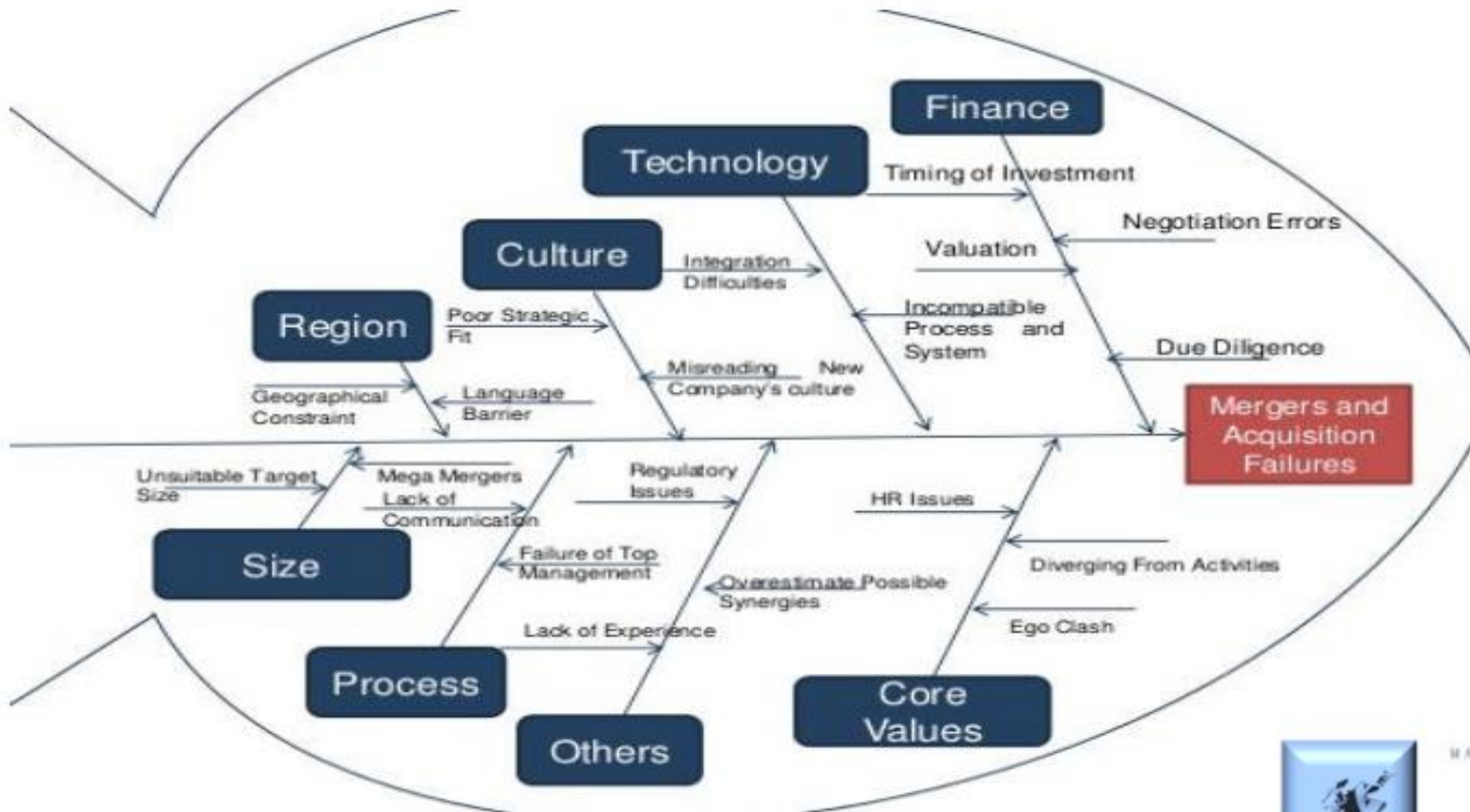
Define Strategies

- Objectives
- Key Strategies
- Short and Long Term Goals
- Operational Plans

Final Reviews

- All Stakeholders
- Review Strategies
- Review Goals
- Review Plans
- Adjust as necessary

Where can the M&A fail?



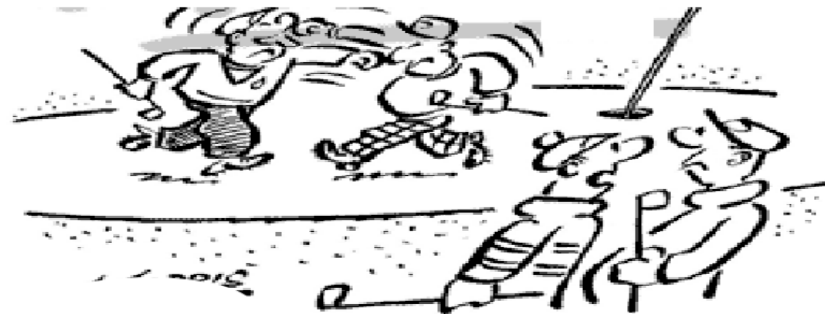
MARKET ANALYSIS



Remember- Merger or Takeover?



No Pain no Gain.



"Does this mean the merger is off?"

Intent



"Joint- Chairmanship?"



MARKET ANALYSIS



There are always Personal Agendas among Directors

Personal Agendas



“What do you say we just skip this whole merger thing and just elope!”



MARKET ANALYSIS



Company Politics, & Personal Agendas

(Management self-interest can kill a Merger before Shareholders get a say)

Company Politics



**"He's had more success in the rat race
than the human race."**



MARKET ANALYSIS



The Board's job is to focus on Shareholders Interests

McKinsey&Company

Source: McKinsey & Co

"There is no point selecting the right Merger Partner, enacting a well- managed and financially robust M&A transaction, only to falter by Baghdad style poor post-merger integration planning. Integrating companies is arguably the most important challenge involving the top of an organization following a merger—appointing the right top team, structuring it appropriately, defining its agenda, and building the trust that enables its members to work well together. Executives who fail to overcome these challenges are responsible for some spectacular failed mergers."

"Successful mergers start at the top, and clients' interests, those of employees, and ultimately shareholders, should all become before self."



The Integration Process needs careful Planning

Management Style



"The role of HR"



MARKET ANALYSIS



Ultimately it comes down to “Leadership”

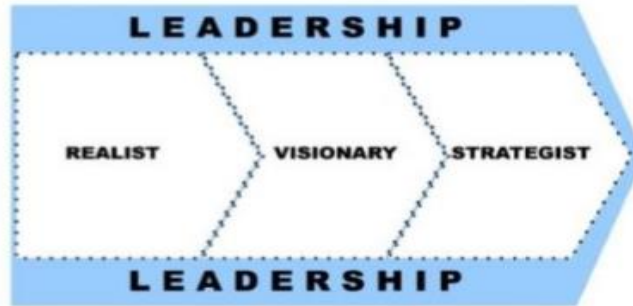
Leadership



**“I completed the leadership course,
So what should I do next?”**



Seeking Effective Industry Leadership



“Britain’s Got Talent”



Recommendation

"The Research in this Report, adequately demonstrates the front-line role M&A has taken in the formation of the leading UK Construction Groups in the past. Industry leaders now need to assess the right Merger and Acquisition decisions for them to become strengthened Groups able to work efficiently on ever larger projects, and seek Re-Capitalisation and funding for investment into higher margin Non-Construction Activities, to compliment and strengthen their Balance Sheets ."



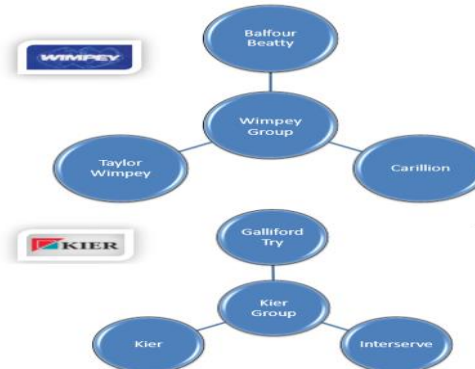
What does the Future hold?

Balfour Beatty

carillion

Interserve

A Few Merger Scenarios



Taylor Wimpey

KIER

Balfour Beatty

carillion

Interserve

Taylor Wimpey

KIER



Who are the Top 8 Merger Candidates?

MERGER SCENARIOS- FINANCIALS (2015)

OVERALL SUMMARY

COMPETITOR	(£M)					(%)				
	MKT CAP (2016)	ENTERPRISE VALUE	NET ASSETS	PENSION DEFICIT	OP CASH FLOW	PFI- DIRECTORS VALN	OP CF/ ENTERPRISE VALN	MKT CAP- NA/ NA	PENSION DEF/NA	PFI/NA
<i>Acquisition Valuation Criteria</i>		<i>A. Enterprise Value= Mkt Cap- Cash +Dbt</i>					<i>B. Pay-Back Ratio (based on Op CF)</i>	<i>C. Premium to Net Assets (Goodwill)</i>	<i>D. Pension Burden (as Ratio to Net Assets)</i>	<i>E. Understated Balance Sheet (Directors Valuation not on Balance Sheet)</i>
BALFOUR BEATTY	1903	2057	826	146	-129	1244	-6.3%	130.4%	17.7%	150.6%
COSTAIN	369	309	121	30	18	na	5.8%	205.0%	24.8%	na
MORGAN SINDALL	318	315	249	-2	36	na	11.4%	27.7%	-0.8%	na
KIER	1308	1461	576	123	170	38	11.6%	127.1%	21.4%	6.6%
CARILLION	1078	1266	1017	406	245	27	19.4%	6.0%	39.9%	2.7%
GALLIFORD TRY	1099	1154	569	35	125	na	10.8%	93.1%	6.2%	na
INTERSERVE	518	840	513	-17	114	na	13.6%	1.0%	-3.3%	na
TAYLOR WIMPEY	4822	4694	2723	180	427	na	9.1%	77.1%	6.6%	na



What are Merger Candidates Strategic Positions?

"While **Balfour Beatty** is focusing on retrenchment and consolidation in its core contracting businesses, it does not have the luxury to do what it needs to do for the longer term, which is to put in place a strategy, and the financing, for future diversification outside contracting."

"**Costain** is an admirable survivor with a "steady as you go" strategy and a brand name that has allowed it to continue to punch above its weight since near demise in the early 1990s. But its days as an independent company are probably numbered now the supportive minority shareholders have diluted their holdings and their nominees have left the Board. With its cash position deteriorating somewhat, and future acquisition aspirations of any substance dawning, surely it's time to seek to be positively acquired by a larger financially robust partner who can help it back into a Tier 1 position it deserves, given its unquestionable engineering capabilities."

"At **Kier**, the fundamentals remain strong (2015/16 Operating Cash Flow was £170m despite its Acquisition write-down problems). They are also one of the few Contractors which maintained Property and Housing Arms. With the indigestion from swallowing May Guerny and the sale of the rump of Mouchel behind them, and operationally more diverse, particularly in Highways, for having done so, maybe Kier should look at a Merger rather than Acquisition for its future growth strategy, outside core UK Infrastructure, Regional Building, and Maintenance and Support Services. Kier itself is now seen as a Major Merger partner itself. It has flirted as an acquisitive company for the first time since the MBO from Hanson, with mixed success. As part of a bigger merged Group, with a similar, albeit smaller, player such as Interserve, better synergies are likely to be realised; or maybe a wider diversification by seeking a partner outside construction and construction services."

"**Carillion**: There are compelling reasons why Carillion should find a large Merger Partner. But focusing just on Balfour Beatty's woes since the failed merger in 2014 does not do justice to both sides of the argument. Two years since the failed buy, Carillion's margins have declined at the operating level. Net borrowings, and Pension Deficit, are higher than expected and a weak pound hurts, as Carillion's private placement borrowing is denominated in US dollars."

"**Galliford** is a strong Diversified Housing and Construction Group with a Market Capitalisation of £1.1bn, a Turnover of £2.5bn, PBT £135m and Net Assets of £600m. It will continue to enjoy a buoyant housing market, and may choose to grow by Merger with another complimentary Group like Countryside, or via Acquisition of Miller Homes, which decided not to list in 2014 as planned, but have shareholders wishing to exit. Galliford is a strong Group with no debt. It could seek to make acquisitions (eg. Interserve or Countryside); or merge with a Group like Kier- if its strategy is to grow via M&A."

"At **Interserve**, Adrian Ringrose has built up a support services business from its roots as Tilbury Douglas. He has had his set-backs like the August 2006 announcement to the London Stock Exchange that accounting issues relating to the mis-statement of accounting balances had resulted in a £30m write-down, But the Group is strong and well diversified. With a Middle East presence as well, and a Pension Surplus unlike its peers, Interserve is a good candidate for merger to form one of the top tier construction groups in the UK. Due to its low Market Capitalisation, it could otherwise become an acquisition target."

"**Taylor Wimpey** is a star performer among current UK Construction Groups, even though it cannot be described in any way as widely diversified. Strong Revenues, Profits, Order Book and a quality Land Bank have earned it a deserved c. £5bn Market Capitalisation. Quite a turnaround from the woes of the Post-Merger company debt Crisis and market downturn it faced in 2007. But the Group needs to look to its longer term future, and its new focus might well be on capitalising on its financial strength to diversify outside its total dependency on the UK Housing Market, despite its current buoyancy and outlook."

"**ACS** (Dragados/Hochtief) strategy for the UK seems to be for measured growth as the company expands its market base with clients such as Network Rail, Transport for London, Highways England, London Underground and HS2. The firm's head count is 246, and based on likely future Project awards, the company might well rank up its plans for the UK. ACS with its financial strength, could conceivably acquire any of the Major 5 Players in the UK, to consolidate its UK position post Brexit. Costain could also be a target."

"**Ferrovial** has Amey well established in the UK, and is itself heavily invested in UK infrastructure concessions, particularly airports. Despite the construction of the third runway at London Heathrow, it is considered unlikely, but not impossible, for Ferrovial to make a large construction company acquisition."

"**BAM** is already established as a Civil Engineering Contractor in the UK. BAM (formerly HBG) also worked extensively with Costain and Carillion (formerly Tarmac) on heavy marine civil engineering projects in the UK like Conway Crossing and Thames Barrier. It is considered not highly likely, but not improbable, that BAM will seek another large acquisition as its M&A route to growth in the UK."

"**Skanska** is well able to acquire a local contractor to bolster its UK presence. Likely target would be Costain with whom it has regularly joint ventured, and was a minority shareholder and potential acquirer in the 1990s / 2000s."

"**Bouygues** M&A- Because of the recent losses, it is less likely that Bouygues is currently seeking to acquire further in the UK, but it has the ability to do so, when it has the will to do so, with major infrastructure projects on the horizon across the UK in coming years."

"Whether **Balfour Beatty and Carillion** should have buried their differences and reconsidered their opportunities to reopen discussions after 6 months is a question unanswered. Several analysts described the abortive merger talks as a missed opportunity. The two chairmen were likely still not talking after the Takeover Panel's six-month cooling period. However, with the change in leadership at Balfour Beatty, maybe it's time to repair relations, and re-open dialogue."



What are Merger Candidate Financial Profiles?

Balfour is to turn-around its Poor Operating Performance on UK Contracts . Its Market Cap is at a 130% Premium to Net Assets, but Balance Sheet seriously understated with the Directors Valuation of PFIs at £1.2bn. That is why John Laing Infrastructure was looking to Asset strip. Balfour needs to MERGE, rather than try to achieve full overhead savings independently Then it can focus on a forward strategy as a leading Construction Group, and achieve target overhead reductions via economies of scale and synergies. If it does not do this, the risk is that it will be acquired by a foreign entity (French, Spanish, Chinese?) and become part of another company's bigger plan, and lose independence.

Costain has deteriorating Operating Cash Flow and Cash Balances. Mkt Cap is more than twice Net Assets, and its Pension Burden is 25% of Net Assets, and growing. Company needs to focus on operational cash flow; and seek a financially strong ACQUIRER to allow it to invest in its Growth and become a Tier 1 Construction Group. Enterprise Val just £300m

Morgan Sindall has same Enterprise and Market Cap Valuation (ie. No debt). Operating Cash Flow has revived, and with Market Cap-NA at 27% premium to Net Assets, and No Pension Deficit, financially the company is a good cheap buy, and will be ACQUIRED if John Morgan becomes a willing seller. Mgmt has significant shareholding; and the company performs in ROI terms. Its profitable fit-out (synergies with ISG?) and urban regeneration businesses may find a buyer. Spending in social housing has its demographic drivers.

Kier's Operating Cash Flow is still good despite extraordinary losses in 2016. It's Pay-Back, Goodwill, Pension Burden Profiles are average, and seems a candidate for MERGER to realise synergistic savings and thereafter focus on diversification. Kier could build on its smaller businesses of Civils, Overseas, Housing or just grow Non-Construction services.

Carillion is a MERGER candidate. It has been selling off PFIs and its Pension Burden at 40% Net Assets is a problem. Operating Cash Flow is still strong at 19% Enterprise Value. Market Cap is only 6% premium to Net Assets but has Intangible Assets on Balance Sheet (ex- Acquisitions). Opportunity to grow into diversified International Group via MERGER.

Galliford Try Market Cap is strong at £1.1bn; has low Net Debt, & a Pension Deficit manageable at £35m. It is a well Diversified Company, but may benefit from building up its Housing Business via ACQUISITION of Miller Homes. It could also consider MERGER with Kier, a Group of similar size, or ACQUIRE Interserve. Depends whether its focus is housing interests or broader diversification as a Contractor/ Support Services Business

Interserve like Costain and Morgan Sindall has a relatively low Acquisition Cost with Market Capitalisation of £518m (similar to Net Asset Value). But unlike the others, it has Debt and Enterprise Value of £840m. It transferred PFIs into its Pension Scheme and it has a Surplus of £17m. Operating Cash Flow is a healthy 13.6% of Enterprise Value, and it has quality overseas businesses across the Middle East and has recently decided to retain its Formwork Subsidiary RMD. Interserve deserves to get on the Growth Train, and its best route is via MERGER or agreed ACQUISITION with a Bigger Player such as Kier, or Galliford. Try.

Taylor Wimpey came from being a heavily indebted Merged Housing Group in a depressed market, to become Market Leader via a large Rights Issue and turn-around of both the Market and the Company's fortunes. Despite being a Cash Hungry acquirer of Housing Land, TW has relatively low Debt. Its Market Capitalisation is at a strong premium to Net Assets, and Operating Cash Flow is acceptable at c. 9% of enhance Enterprise Value £4.7bn. Taylor Wimpey is a star performer among its Construction Group Peers, but cannot be described as widely diversified, with all its business in UK Housing. Its heritage was more diversified. Its Market value recognises its strong Profitability, Land Bank, Order Book, rather than being the Net Present Value of a less certain long-term cash flow model in a traditionally very cyclical market. The opportunity is for TW to use its Financial muscle, borrowing power, and diversify via M&A. Its 14,000 units per year in UK is probably at a maximum for profit sustainability for a short landbank volume builder. Its M&A growth options are however exciting.



Scenarios of Mergers (& Company Combinations)?

MERGER SCENARIOS- FINANCIALS (2015)

TOP 10 COMBINATION SCENARIOS

MERGED SCENARIOS <i>(assuming no premium to Mkt Cap)</i>	(£M)					(%)		
	MKT CAP	ENTERPRISE VALUE	NET ASSETS	PENSION DEFICIT	OP CASH FLOW	OP CF/ ENTERPRISE VALN	MKT CAP- NA/ NA	PENSION DEF/NA
BALFOUR/ CARILLION	2981	3323	1843	552	116	3.5%	61.7%	30.0%
KIER/INTERSERVE	1826	2301	1089	106	284	12.3%	67.7%	9.7%
GALLIFORD/ INTERSERVE	1617	1994	1082	18	239	12.0%	49.4%	1.7%
GALLIFORD/ KIER	2407	2615	1145	158	295	11.3%	110.2%	13.8%
MORGAN SIND/INTERSERVE	836	1155	762	-19	150	13.0%	9.7%	-2.5%
TW/BALFOUR/ CARILLION	7803	8017	4566	732	543	6.8%	70.9%	16.0%
KIER/CARILLION/GALLIFORD	3485	3881	2162	564	540	13.9%	61.2%	26.1%
KIER/CARILLION/INTERSERVE	2904	3567	2106	512	529	14.8%	37.9%	24.3%
GALLIFORD/KIER/INTERSERVE	2925	3455	1658	141	409	11.8%	76.4%	8.5%
KIER/GALLIFORD/TW	7229	7309	3868	338	722	9.9%	86.9%	8.7%



Profiles of Potential Merged Groups (& some Company Combinations)

Balfour Carillion would have the largest Pension Deficit to Net Asset Ratio, and lowest Operating Cash Flow to Enterprise Value (but takes no account of restored BB Operating Cash Flow or Synergistic OH savings) The Group would be the largest & most diversified (non-housing) UK Construction Group with combined businesses in Construction, Support Services, & over £1.3bn PPPs in UK, North America & Middle East.

Kier Interserve would have the second lowest Pension Burden and highest Operating Cash Flow to Enterprise performance Ratio. It would be similar in Value to the current Balfour Beatty model, but very different in operations, K/I would derive profits from Interserves Support Services and Equipment Services, complementing Kier's Regional Building Business and Highways Maintenance business, but be seen as an Acquisition by Kier.

Galliford Interserve combined would have a Market Capitalisation lower than Balfour Beatty, but higher Net Debt at £350m, less scope for growth, but provide Galliford with an established non-construction Support Services Arm

Galliford & Kier are similar businesses in size and both in Construction, Housing and PPPs, Kier having a large Services offer. Combined Enterprise Value would be £2.6bn, larger than any current Contractor.

Morgan Sindall/ Interserve would have the lowest absolute Pension Deficit and Ratio to Net Assets. It would also have the second highest Operating Cash Flow to Enterprise Value, and lowest Goodwill, making it an attractive tie-up based on the numbers. But operationally the Combined Group would have the same Enterprise Value as the current Galliford Try, and take Interserve back into more general contracting, Fit-Out and Partnership Housing which it might not consider its focus for diversification

The Combined Group of Businesses of Taylor Wimpey, Balfour Beatty and Carillion would produce a c.£8bn Market Capitalised Construction Group and clear market leader with next to no Gearing, a mature 'stand-alone' Housing Business with less appetite for net cash consuming growth, and a Balance Sheet to enact a broad Diversification programme to rival European Major Competitor Groups. The Group would be able to manage its considerable combined Pension Deficit of £730m, and generate likely well in excess of £750m Operating Cash Flow, once Balfour Beatty / Carillion merged Synergies are derived, and Balfour Beatty's contracting returns to Profit.

The Combined Group of Businesses of Kier, Carillion and Galliford would produce a larger Contractor/ Support Services and Housing mix with a c. £4bn Enterprise Value with £540 Annual Operating Cash Flow (second highest ratio to Enterprise Value at 13.9%), but a 26% Pension Deficit to Net Asset Ratio.

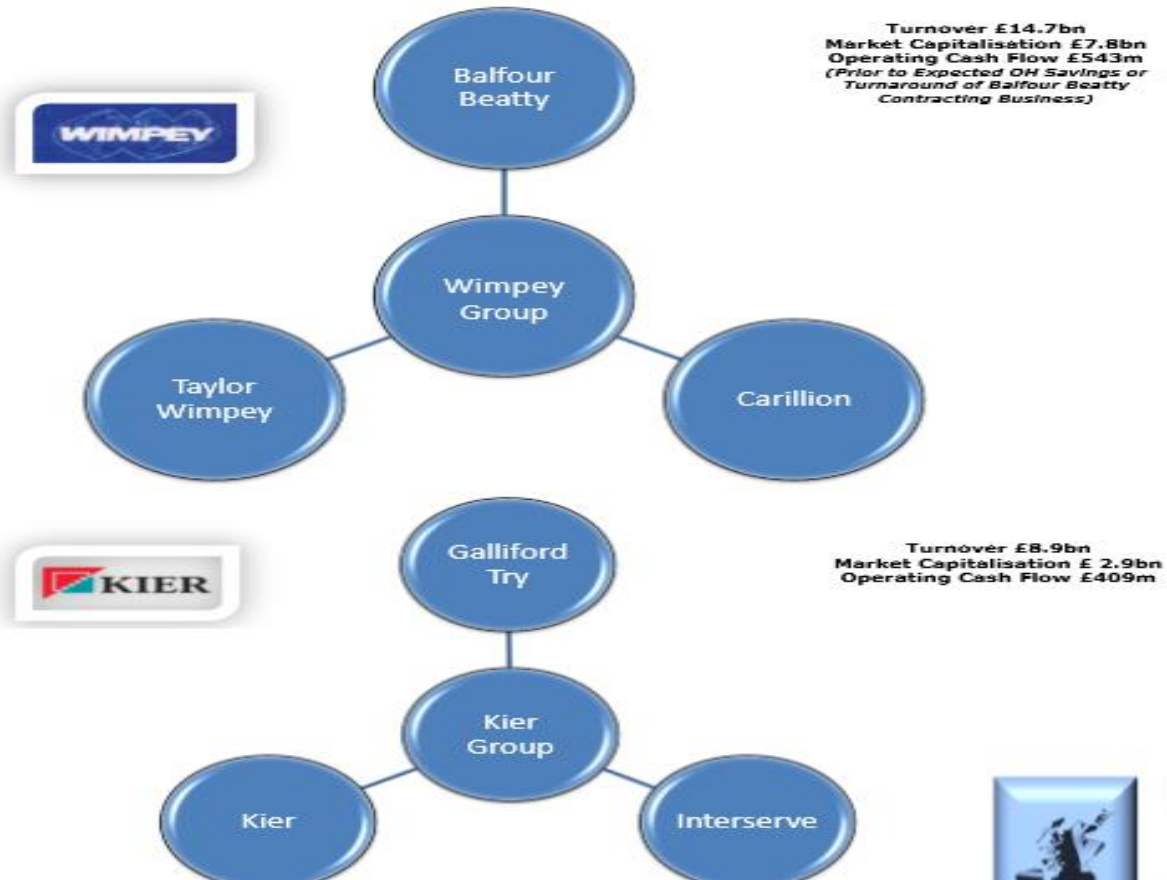
The Combined Group of Businesses of Kier, Carillion and Interserve would have a similar Pension Burden Ratio, but have higher Gearing and lower Market Capitalisation (albeit at lower Goodwill to Net Assets). But it would have a good balance of Construction to Support Services mix (£4.6bn Tnd £5.7bn Turnovers, respectively), and highest Operating Cash Flow to Enterprise Value of 14.8%.

The Combined Group of Businesses of Kier, Interserve and Galliford would have a nominal Pension Deficit, but poorer Pay-Back and Goodwill comparisons. However, it would provide an excellent mix of Construction, Support Services and Housing Businesses (c. £4bn, £3bn & £1.5bn) and rival The TW/BB/Carillion combination in market dominance in its sectors, excluding certain infrastructure sectors such as Carillion & Balfour's combined Rail; and Power, etc.

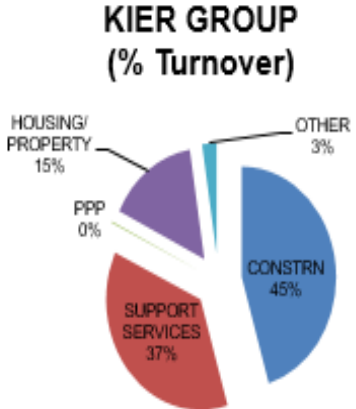
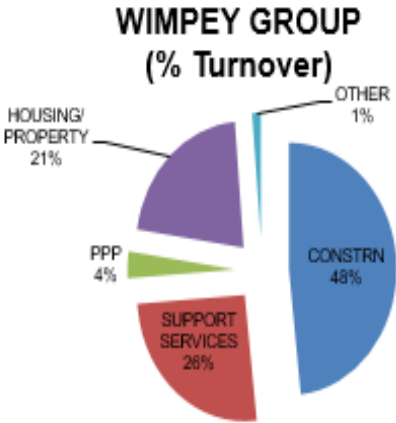
The Combined Group of Businesses of Kier, Galliford and Taylor Wimpey would have the targets Housing Business of the comparisons but one of the lowest percentage (at £1.2bn) mix of Support Services, so not be the most obvious Merger to produce a well diversified Group.



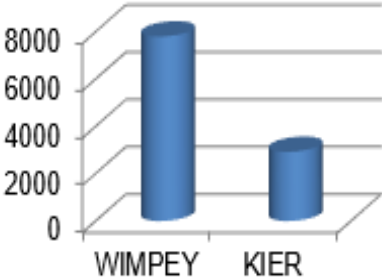
Two leading Merged Combinations Emerge



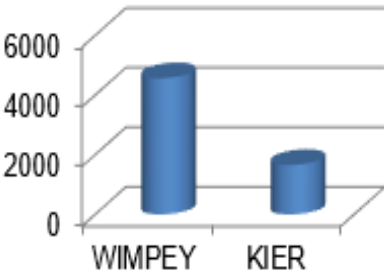
Current Stats of those leading Combination Groups



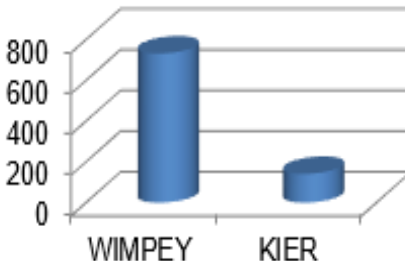
MKT CAP



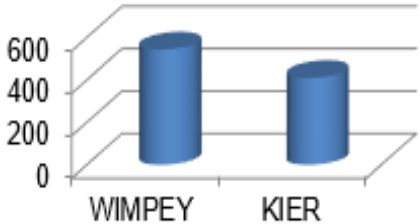
NET ASSETS



PENSION



OP CASH FLOW



What would be the Resultant European Rankings?

Ranked by Turnover

€M

Rank	Company		Sales	Market Capitalisation	EBIT	EBIT %
1	VINCI	FR	38,518	34,801	3,758	9.8%
2	ACS	SP	34,925	8,501	1,439	4.1%
3	BOUYGUES	FR	32,428	12,613	941	2.9%
4	TW/ BB/CARILLION	UK	22,279	13,269	1,158	5.2%
5	SKANSKA	SWE	16,363	7,373	672	4.1%
6	EIFFAGE	FR	14,060	5,493	1,431	10.2%
6	STRABAG	AUS	13,123	2,419	341	2.6%
7	GALL/KIER/ INTERSR	UK	12,474	4,949	358	2.9%
na	BALFOUR BEATTY	UK	11,633	2,528	-251	-2.2%
8	FERROVIAL	SP	9,701	15,270	901	9.3%
9	BAM	NETH	7,423	1,387	-11	-0.1%
10	NCC	SWE	6,681	3,088	325	4.9%



And the Global Rankings Scenario?

Ranked by Turnover

Rank	Company		Sales	Market Capitalisation	EBIT	EBIT %
1	CHINA STATE	C	126,278	26,981	6,752	5.3%
2	CHINA RAILWAY CONSTFC	C	86,120	15,496	2,382	2.8%
3	CHINA RAILWAY GRP	C	86,034	15,978	6,982	8.1%
4	CHINA COMM (CCC)	C	57,880	15,212	3,700	6.4%
5	VINCI	FR	38,518	34,801	3,758	9.8%
6	ACS	SP	34,925	8,501	1,439	4.1%
7	BOUYGUES	FR	32,428	12,613	941	2.9%
8	ODEBRECHT	BRA	34,448	na	4,760	13.8%
9	CHINA METALLURGICAL	C	31,165	5,310	852	0.027338
10	TW/ BB/CARILLION	UK	22,279	13,269	1,158	5.2%



MARKET ANALYSIS



Global Ranking by Company Value (cont'd)

Ranked by Market Capitalisation

Rank	Company		Market Capitalisation	(Europe Rank)	
1	VINCI	FR	38,518	34,801	1
2	CHINA STATE	C	126,278	26,981	
3	CHINA RAILWAY GRP	C	86,034	15,978	
4	CHINA RAILWAY CONSTR C	C	86,120	15,496	
5	FERROVIAL	SP	9,701	15,270	2
6	CHINA COMM (CCC)	C	57,880	15,212	
7	TW/ BB/CARILLION	UK	22,279	13,269	3
8	BOUYGUES	FR		12,613	
9	BARRATT	UK	4,931	8,625	
10	ACS	SP	34,925	8,501	



Global Rankings by Profit & Profitability (cont'd)

Ranked by Market EBIT

Rank	Company		Sales	Market	EBIT	EBIT
1	CHINA RAILWAY GRP	C			6,982	8.1%
2	CHINA STATE	C			6,752	5.3%
3	ODEBRECHT	BRA			4,760	13.8%
4	VINCI	FR			3,758	9.8%
5	VINCI	FR			3,758	9.8%
6	CHINA COMM (CCC)	C			3,700	6.4%
7	CHINA RAILWAY CONSTR C				2,382	2.8%
8	ACS	SP			1,439	4.1%
9	EIFFAGE	FR			1,431	10.2%
10	TW/ BB/CARILLION	UK			1,158	5.2%



Seek the best Corporate Advice

The BIG 4



My Business Analyst.



"In six more weeks, these MBAs will be ready for market."

Corporate Advice

**Think Different.
But not different from me.**



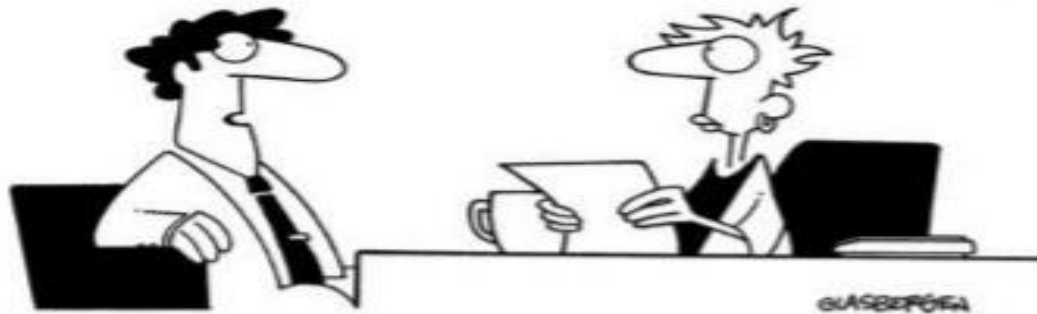
"Advisers advise, Managers Decide."



www.thinkbigpartnership.com

At the End of the Day- “It’s a People Business”

People Management



**“Yes, I think I have good people skills.
What kind of idiot question is that?”**



MARKET ANALYSIS



Whose move next?



Peter Redfurn, CEO Taylor Wimpey

THANK YOU





FOR MORE INFORMATION VISIT US ONLINE
**FREE
ISSUE**
www.constructionmagazine.com

