

Business Services: Sector Review Q1-Q3 2023

Market Overview

Macro Overview

Early signs of recovery seem to be appearing across the UK economic horizon. Recent data is showing a deflationary path as headline CPI has reduced significantly from its peak of 11.1% in October 2022, to 6.7% in August. Looking ahead, with September forecast at 6.5%, it is likely that the CPI will be in a slow decline towards the end of the year.

Considering these promising signs, the BoE's decision not to proceed with another 25-50 basis point rise to the bank rate will come as a relief to many. Governor of the Bank of England, Andrew Bailey, however, has commented saying that "we [the bank] will continue to do whatever is necessary" when discussing its policy decisions, which certainly leaves the door open for further rate rises if the CPI does not continue to demonstrate progress in the return to the 2% CPI target.

This extended period of high inflation and interest rates has placed significant downward pressure on GDP and economic recovery as both consumers and businesses limit spending when faced with more volatile markets and hostile borrowing conditions.

During Q2 2023, the economy did manage to grow slightly according to ONS estimates but Q3 and Q4 were predicted to flatline leading to an overall growth of 0.4%. This flatline is likely to be partly attributed to drag following the expiration of fixed rate mortgages and the decrease in imports and exports due to weak global demand and the continuing effect of Brexit.

Valuation and Deal-Making Impact

Deteriorating macro conditions over the past 12-18 months have resulted in a general decline in both public and private valuations, lower levels of investment across all sectors and a decline in deal-making in general, be that in trade deals or private equity buyouts; the business services sector is no different. The sector is, however, expected to regain its resilience throughout Q4 as the market settles into a less inflationary journey.

Companies in this sector provide services that are embedded in their clients' operating models. With loyal client bases and strong repeat revenues, specialist companies often attract significant interest from PE firms, interest which has remained high through this period of higher interest rates due to the low capital requirements needed to trade. This can help drive strong returns on invested capital.

As the economy focuses on digital transformation and sustainability/ESG goals, expertise will be in demand to help facilitate the transitions. Against a more challenging backdrop, the use of data and digital processes will be increasingly required to help clients remain competitive and indeed make significant gains. While businesses generally intend to make sustainability policies and goals a priority, many lack the resources or expertise to successfully create and implement a workable plan. As ever, when there is a new business shift, there is a great opportunity for those in business services with the requisite expertise to leverage. More established consultancy firms are therefore looking to acquire niche specialisms to cover areas where they perceive themselves to be light, relative to the expected market demand.

Top Trends:

Labour force

Attracting and retaining talent has been challenging in post-Brexit UK throughout all sectors, with the hardest hit companies having largely labour-led models that proliferate large parts of the business services sector. Consequentially, companies have begun to explore methods to increase staff retention, commonly including flexible working hours and development programs for staff. The challenge is to do this whilst retaining, or preferably improving, levels of productivity, which have fallen behind in the UK, particularly post-Covid as increasing numbers of staff seek to secure some level of homeworking.

Labour-led models, particularly those linked to specialist expertise, do continue to attract investment - provided investors can see growth not being impeded by associated labour shortages.

AI, data collection and tech

We have seen a huge growth in AI take-up, particularly across the consulting sector with companies such as Infosys and McKinsey developing dedicated AI divisions to boost productivity and efficiency company wide. Business services increasingly sees tech innovation as a “must-have” to operate efficiently, ensure scalability internally and convince clients of their ability to fully support rapid growth.

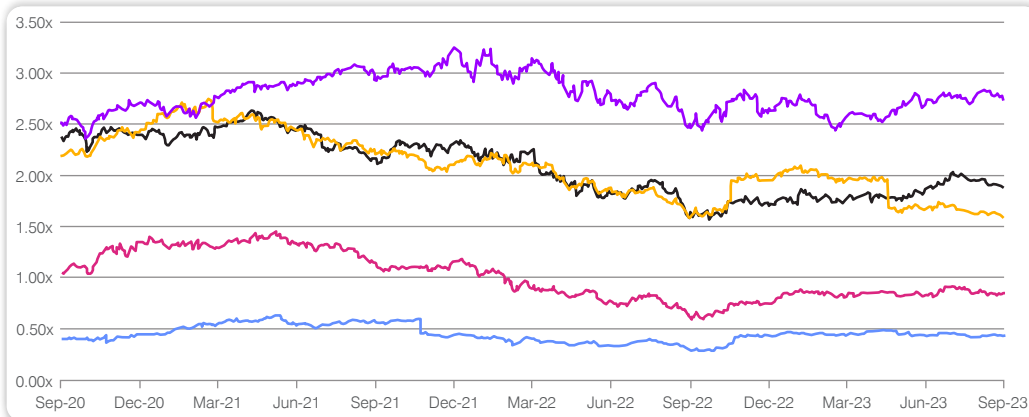
ESG/Sustainability

Over the pandemic, many businesses reassessed their models, which enabled investment and encouraged a focus on sustainability. Resilience within the sector has ensured a commitment to ESG and sustainability has been maintained over a low investment and high-interest period. Sustainably-focused companies have maintained growth, whilst global conglomerates are following suit and striving to foster an ESG-aligned workforce, particularly as new reporting regulations come into increasing focus, with recent high profile “green-washing” cases highlighting the costs of non-compliance.

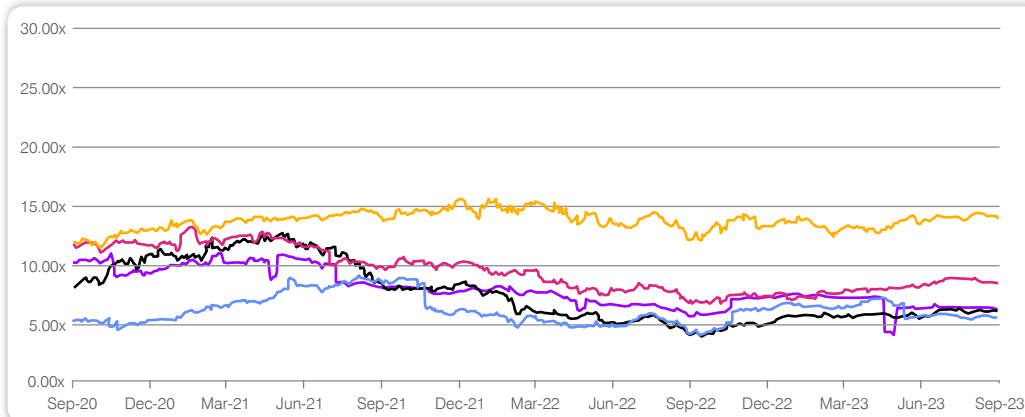
The UK government's recent policy changes, which will hinder the rate at which the UK achieves its net zero goals, have put some level of uncertainty around timing at the very least. We do not, however, see the general direction of travel reversing and the changes have not, at least yet, altered business' commitment to a more sustainable workplace. Whilst the announcements may cause some delay in investment programmes as businesses try to work out the real timelines, overall we expect that those already invested will trust in the ultimate goals and press forward, while those that have fallen behind may breathe a sigh of relief and try to use the delay to catch up. Certainty would obviously help all round.

Market Valuations

EV/Revenue Multiples



EV/EBITDA Multiples



Source: S&P Capital IQ as of 27 September 2023

— Facilities Management — Construction — Marketing & Communications — Consulting & Professional Services — Logistics, Import & Distribution

Current Multiples	Facilities Management (7)	Construction (18)	Consulting & Professional Services (26)	Logistics, Import & Distribution (51)	Marketing & Communications (38)
Public Revenue Multiples	0.80x	1.10x	1.80x	1.20x	1.10x
Private Revenue Multiples	1x-3x	1x-3x	1x-3x+	0.5x-1x	1x-2.5x
Public EBITDA Multiples	6.70x	6.10x	11.20x	6.00x	8.50x
Private EBITDA Multiples	5.5x-7.5x	7x-9x	6x-12x	3x-6x	4x-7x

Due to the reduction in the level of cheap debt, alongside concerns over interest rates, revenue and EBITDA multiples have fallen from 2020 levels across all sectors, as buyers have sought to account for the extra cost of financing. There is cash available, and the demand for deals, particularly in the consulting and professional services subsector, remains high, with strong competition for premium assets.

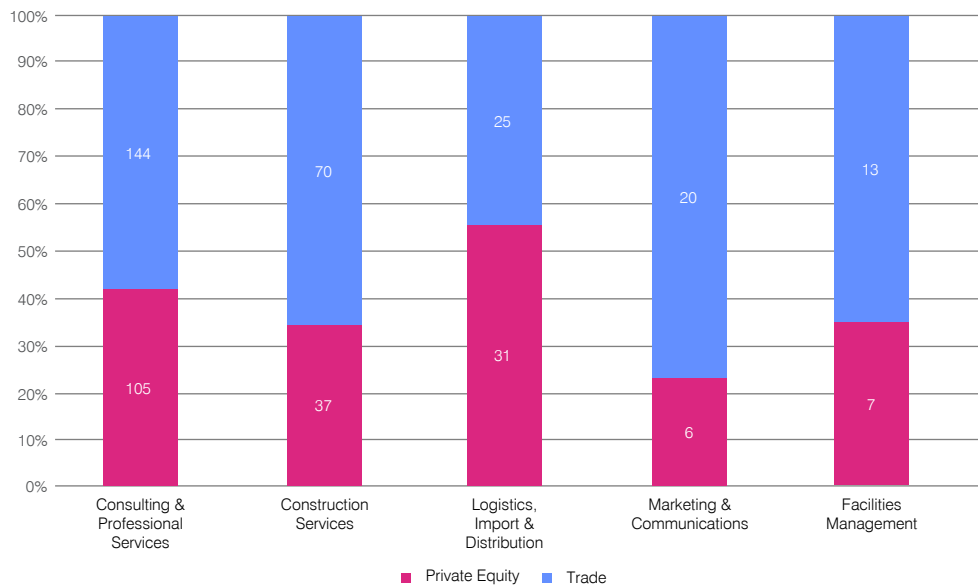
Facilities management and construction services remain at the lower end of both revenue and EBITDA multiples, due to their labour-led model and lack of tech and AI development to promise greater efficiency. There is nonetheless steady demand for such services, ensuring they continue to appeal to investors. Sector multiples are predicted to remain steady, despite the reliance on a productive workforce, which remains a challenge.

The marketing and communications sector has inevitably shown some variation in the multiples it has attracted, with the pandemic and now recessionary/stagnation pressures causing cutbacks in spending on what is sometimes seen as more discretionary expenditure. The key variable here is when and at what level buyers believe normal trading will resume. Nonetheless, businesses do need a strategy and associated expenditure to support operations, and we are starting to see some rebound in trading, albeit some businesses have reassessed where they are spending their advertising dollar.

Revenue multiples spiked in the sector during the lead up to the coronation, with the expectation of increased advertising spend by businesses to support the hospitality and retail sector over the period.

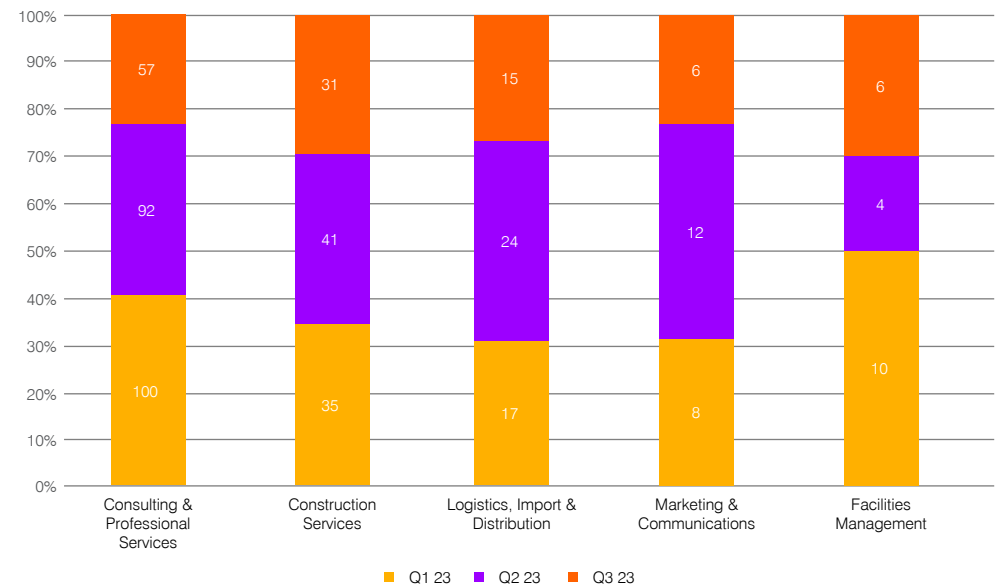
M&A Activity

Q1-Q3 2023 Trade vs Private Equity Buyout Activity



Source: PitchBook

Q1-Q3 2023 Business Services Subsector Breakdown



Source: PitchBook

- Deal volume fell by 50% compared to last year, from 244 deals in Q3 22 to 122 deals in Q3 23. Deal value dropped 90% from c. £11bn in Q3 22 to c. £1bn in Q3 23. A reduction in the availability of cheap debt as interest rates rose resulted in companies focusing on their internal structures, rather than looking to expand through M&A opportunities.
- The consulting and professional services subsector has made up the largest portion of deal volume throughout 2023 so far, having seen slightly more investment from trade parties than PE. Such services continue to be in demand as businesses seek to understand and plot a path through uncertainty, and providers look to consolidate to bring additional skills in-house.
- Although the volume of deals has dropped overall, with fewer sellers coming to the market, private equity activity increased relative to overall deal activity from 34% in Q2 23 to 38% in Q3 23, driven by growth in the sector and robust repeat revenues, supported by specialist knowledge that business services companies offer.

Active Buyers & Investors

Active Investors/PE-Backed Trade

- ◆ BGF was the most active investor in the past 12 months, acquiring consulting companies in the sustainability and environmental consulting space through its platform investment, RSK.
- ◆ Exponent Private Equity is also adding bolt-ons, for its platform investment in business advisory and accountancy Xeinadin.

Active investors in the past 12 months	Platform	Number of Investments
	RSK Group	9
	Xeinadin Group	6
	Perspective Managing Wealth	3
	Dains Accountants	3
	TSA Management	2
	CH & Co	2
	Opus Safety	2
	Phenna Group	2
	Broadstone Corporate Benefits	2
	Shaw Gibbs Group	2

Source: PitchBook

Active Acquirers

- ◆ Marshall Fleet Solutions has been the most active acquirer in the past 12 months. Its acquisitions support Marshall's broader Ambition 2030 programme which is focused on developing sustainable products and services to help customers meet their climate action targets.
- ◆ There is significant consolidation in the business services sector, particularly in the consulting and professional services subsector, with both PE houses and trade buyers acquiring companies that offer niche expertise and entry into new markets.

Active acquirers in the past 12 months	Number of acquisitions
	3
	2
	2
	2
	2
	2
	2
	2
	2
	1

Source: PitchBook

Selected Transactions - Private Equity

Deal Date	Seller	Subsector	Description	Buyer	Deal Size (£m)	Revenue Multiple	EBITDA Multiple
July 2023	More Telemarketing	Marketing & communications	Livingbridge backed, Jensten Group acquired More Telemarketing, a specialist insurance telemarketing operator serving small and medium-sized enterprises and corporate clients. The deal was one of two deals completed in the same week and allowed the MD of More Telemarketing to step into a new role as lead generation director. Details of the transaction were not disclosed.	Livingbridge/Jensten Group	N/A	N/A	N/A
July 2023	Sureserve Group	Construction services	French PE firm, Cap10 completed a public-to-private acquisition of LSE listed Sureserve, a provider of mission critical compliance and energy support services. Cap10 has already indicated that they are planning to pursue accelerated growth through M&A without the costs and regulation of a listed company.	Cap10 Partners	214	0.74x	8.3x
April 2023	Xpediator	Logistics, import & distribution	BaltCap, the largest PE firm in the Baltics completed the first public-to-private acquisition by a Baltic investor in their purchase of AIM listed Xpediator, an integrated freight management business operating in the supply chain logistics and fulfillment sector across the UK and Europe. The consortium of investors will aim to boost the core freight-forwarding offers in Europe and internationally while developing the UK based business.	A consortium of investors led by Baltcap	62	0.16x	6.7x (EBIT)*
April 2023	APS Security & Fire	Facilities management	Obseuio Group, backed by Beechtree Private Equity, acquired APS Security & Fire a design, installation and maintenance of intruder and fire systems. APS was the first acquisition following Beechtree's investment to support both the organic and inorganic growth strategy of the business.	Beechtree Private Equity/Obseuio Group	N/A	N/A	N/A
April 2023	Security Watchdog/ Capita PLC	Consulting & professional services	Bridgepoint backed Matrix, acquired Security Watchdog, a pre and post-employment screening solutions provider from Capita PLC. Security Watchdog, which is the largest EMEA supplier of background checks and a trusted partner to clients across the globe, was sold by Capita as it no longer formed a part of their core growth strategy and would support the strengthening of Capita's balance sheet.	Bridgepoint Deveopment Capital/Matrix	14	0.51x	8.0x <i>(Estimated based on 1.5m PBT)</i>

*EBIT multiple has been shown for Xpediator/BaltCap as it is considered more reflective of cash generation, given high levels of depreciation and hence ongoing capex.

Source: PitchBook

Selected Transactions - Corporate

Deal Date	Seller	Subsector	Description	Buyer	Deal Size (£m)	Revenue Multiple	EBITDA Multiple
September 2023	Buckingham Group Contracting (Rail Division)	Construction services	Sold following significant cashflow pressures and losses incurred. The rail division and HS2 contract were passed on to Kier Group, safeguarding the jobs of 180 people. Kier Group's acquisition has allowed the company to access core markets, giving them a new potential to accelerate their medium-term value creation plan.	Kier Group	9.6	N/A	N/A
July 2023	RIA Consultants	Consulting & professional services	The fast-growing nature of RJA complements the existing expertise within Gateley Legal's construction and residential development teams. RJA's services to the UK property insurance market will strengthen Gateley's leading position in the sector.	Gateley Legal	6	1.64x	7x (£0.8m PBT)
April 2023	AA Projects	Facilities management	The acquisition positions Drees & Sommer into the UK and Irish markets, whilst also allowing for a new joint focus on geographic expansion into the North American Market. Drees and Sommer will benefit from AA Projects strong UK reputation and client base in the public and private sectors, whilst AA Projects believes the partnership will help in delivering long term sustainability and growth.	Drees and Sommer	N/A	N/A	N/A
February 2023	The Social Chain	Marketing & communications	Initial consideration of £7.7m and potential future payments of £9.5m dependent on performance. A notably high EBITDA multiple would appear linked to securing CEO Steven Bartlett into the leadership team, giving Brave Bison instant coverage and recognition, helping in aligning a sustainable business trajectory. The Social Chain has a global presence which will increase Brave Bison's presence across three continents, helping in the development of global campaigns for brands such as Amazon, TikTok, KFC and New Balance.	Brave Bison Group	7.7 (Initial Consideration)	0.81x	13.1x
February 2023	McBurney Transport Group	Logistics, import & distribution	The acquisition aligns with McBurney Transport Group's strategic focus on cold chain logistics, overlapping with existing activities in the region. Offering opportunities to work with other parts of DFDS' pan-European transport network, operational synergies are expected to contribute to benefits and optimise network utilisation.	DFDS	135	0.94x	6.1x

Source: PitchBook

Polestar Sector Deals

<p>Sustainability Exit</p> 	<p>Business Services Exit</p> 	<p>Business Services Exit</p> 	<p>Business Services Exit</p> 
<p>Sustainability MBO</p> 	<p>Business Services Debt Advisory</p> 	<p>Business Services M&A</p> 	<p>Business Services M&A</p> 
<p>Sustainability Exit</p> 	<p>Software, Media & Technology Exit</p> 	<p>Software, Media & Technology Exit</p> 	<p>Software, Media & Technology Exit</p> 