

THE OC&C TIC 101  
INDEX 2015



# TIC-TOCK

Calling time on buy and build for scale's sake in the  
Testing, Inspection and Certification market

# SUMMARY

Testing, Inspection and Certification (TIC) services has been a highly attractive market on the agenda of major investors across the globe. However, growth rates have declined significantly since 2012, with average growth of 11-16%pa dropping down to just 6% in 2014. Oil & Gas and Mining are no longer powering the sector, and M&A is proving increasingly hard to exploit.

Rising customer expectations are a key factor behind who's winning and who's losing. Global Sector Champions are winning, leveraging deep sector knowledge with increasingly demanding customers; Local Leaders are lagging behind as they struggle to serve customers who want to consolidate spend with suppliers who can serve them at a multi-country level.

Critically, pure scale is no longer a winning proposition. M&A remains important, but increasingly as a route to drive organic growth, by offering an expanded range of capabilities to serve key customers.

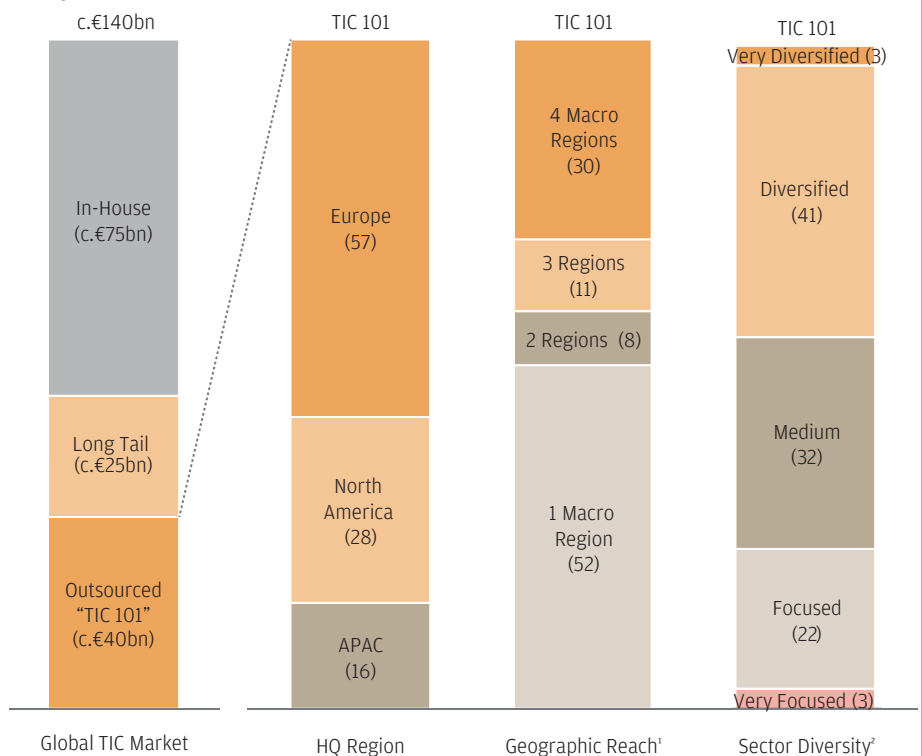
Four fundamental levers to delivering organic growth are

- Creating a customer centric organisation to grow share of wallet in key accounts
- Investing in both capex and opex to better reach and serve client needs
- Automating processes through the intelligent use of technology
- Finding and growing technical expertise

## THE TIC 101

OC&C's "TIC 101" Index is our proprietary database of the leading 101 TIC players across the globe. Our first TIC Index was produced in 2014. We have now updated the analysis in order to take stock of recent changes

### Composition of the TIC 101



1. Presence in four macro regions Europe, North America, APAC, Rest of World  
 2. Very Diversified = 13+ sector verticals covered, Diversified = 7-12, Medium = 5-6, Focused = 3-4, Very Focused = 1-2

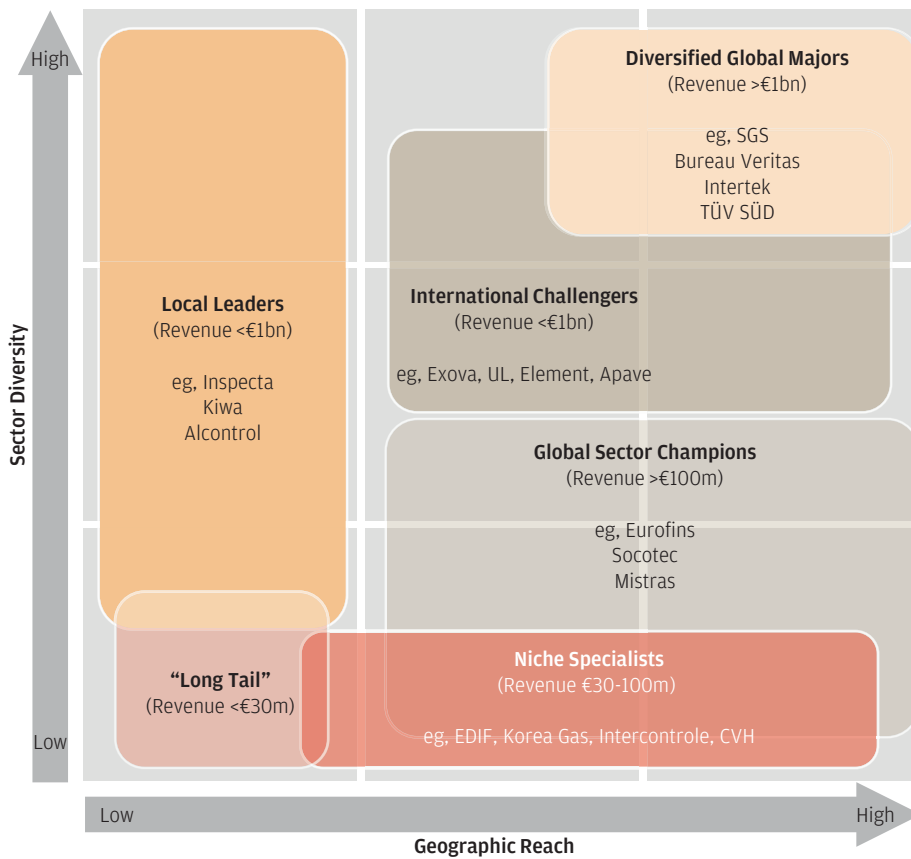
# WORTHY OF INSPECTION

The TIC market is large, diverse and full of opportunity - and yet under-reported and often misunderstood by analysts and investors:

- c.€65bn outsourced global market (at least)
- Average EBITA margins over 14% for the past 5 years
- Growth in the high single digits since 2010
- Over 50 M&A deals involving companies in the TIC 101 in 2014-15

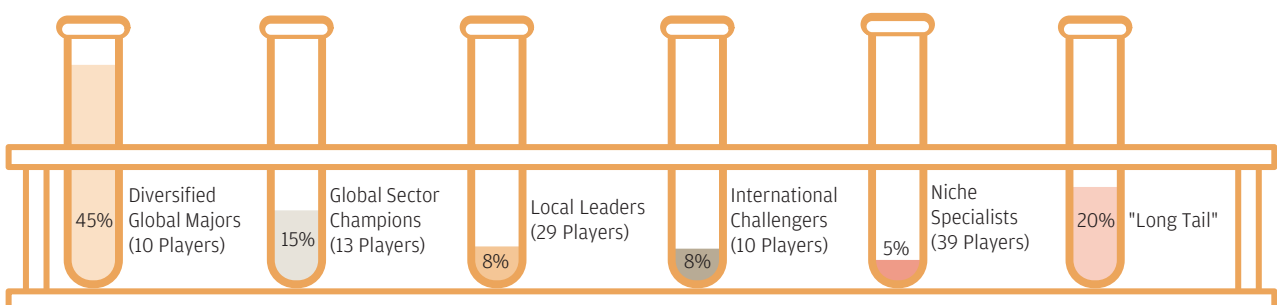
There is also not one type of TIC player - the traditional scale-based terms “Tier 1” and “Tier 2/3” are insufficient in our view - the right lens for understanding this market is one which reflects the level of sector diversification and geographic reach.

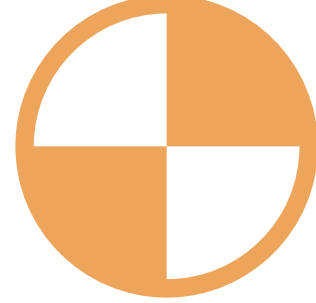
## TIC Market Classification and Leading Players



## Revenue Covered by TIC Market Classification

Total Outsourced Market





# TESTING TIMES

Growth rates have seen a significant slowdown since 2012, with average growth of 11-16%pa (including M&A) dropping down to just 6% in 2014.

## We see three main factors behind the slowdown in growth:

- **Sharing the pain with end customers**  
Historical powerhouses of growth such as Oil & Gas and Mining have significantly faltered in the last 2 years, driven by global oil and commodity prices. Some subsectors have seen drops in demand of up to 50%, with resulting oversupply hitting both volume and price
- **Rising customer expectations**  
Customers are becoming more demanding - they are actively looking to consolidate their spend across suppliers, but in return they are looking for consistently high levels of responsiveness, accuracy, and communication. The standard has been set in other more mature outsourcing industries where dedicated account managers alongside customer portals with integrated service reports are often the norm
- **Diminishing returns on M&A**  
Until recently, most companies achieving high revenue growth have done so through M&A, which has contributed c.30-60% of revenue growth for leading players in recent years. However this is increasingly hard to exploit: M&A targets of the requisite size are increasingly scarce and expensive; the multiples demanded are high, such that simple corporate finance logic (multiple arbitrage) will not justify the acquisition alone

## No more buy and build for scale's sake

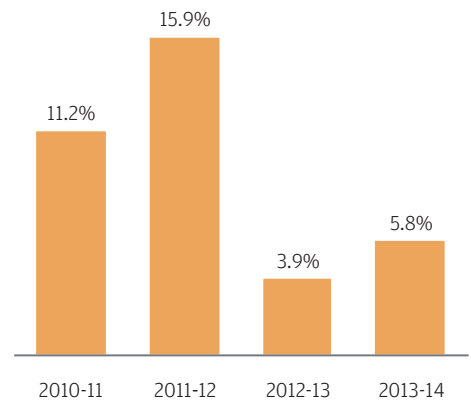
Traditionally, a simple strategy of buy and build, regardless of where footprint was added, allowed companies to rise with the tide of the market.

The combination of rising price expectations and market headwinds has put an end to this.

Indeed, pure scale is no longer a winning proposition.

- Being a highly diversified and large business can be a detriment to a company's growth due to the stretch of management bandwidth and resources and a diluted level of customer understanding
- The highest growth rates are seen in companies with a reasonable degree of sector coverage, but without over-stretching
- Similarly, over-stretching geographically can be a strain, although in general a more global offering supports higher growth

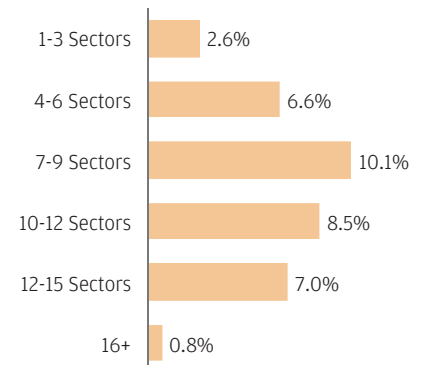
**Average Revenue Growth of TIC 101**  
% YoY (Including M&A)



**TIC 101 Revenue Growth**

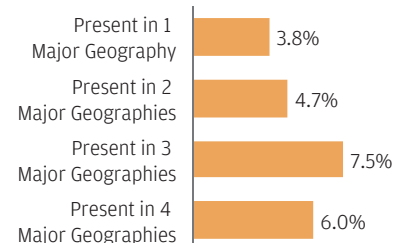
### By Sector Presence

% Growth 2013-14



### By Major Region Presence

% Growth 2013-14



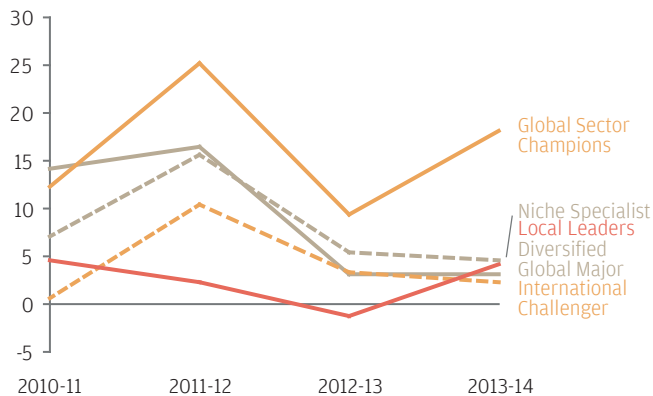
# WINNERS AND LOSERS

## Global Sector Champions are winning

- Their growth has been driven in part by M&A, where increasingly a demonstrable sector platform helps the acquirer win the auction
- They have also been utilising deep sector knowledge to:
  - Gain the trust of clients
  - Increase share of wallet as customers move to consolidate spend
  - Grow the size of the market through outsourcing deals

## TIC Provider Performance by Type, 2010-14

YoY % Revenue Growth (Weighted Average)

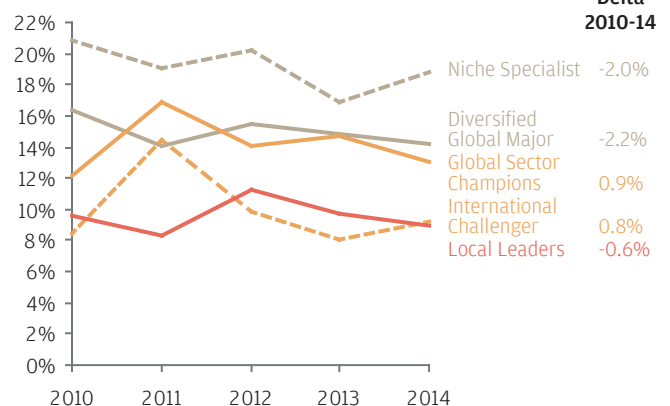


## Local Leaders are lagging behind

- They have the lowest EBITDAs and the lowest growth in the industry, and were the only group to experience a contraction in size in 2013
- Our experience suggests that this is primarily born of an inability to serve customers who are increasingly looking to consolidate their spend towards suppliers who can serve them at a multi-country level
- All too often this is compounded by a lack of leadership within their local end-markets, meaning investments in proposition and sales are spread too thinly across customers

## EBITDA

% Margin (Weighted Average)



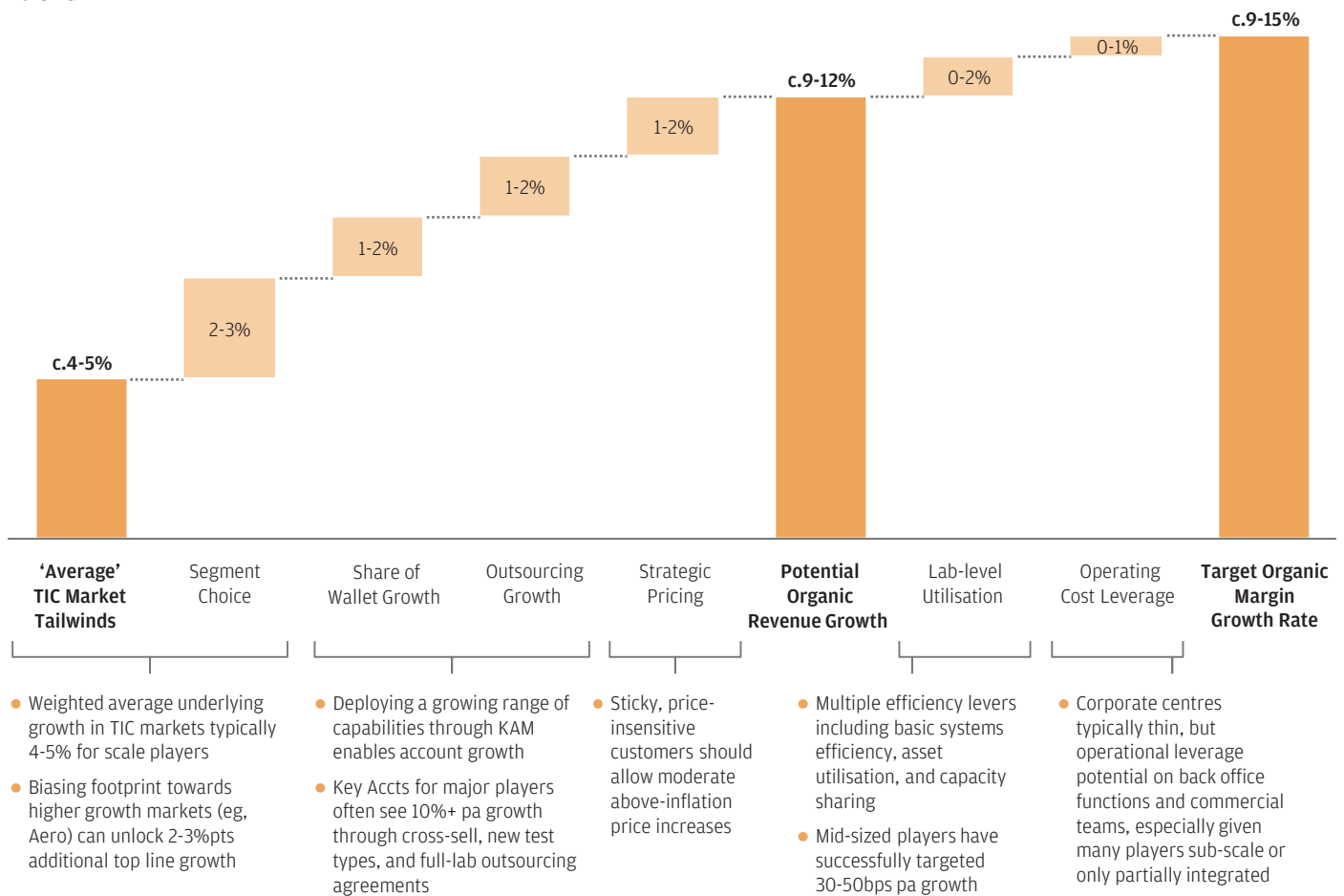


# PLANET ORGANIC

TIC players are increasingly reliant upon organic growth to achieve their goals. Although “rising with the tide” in the market still provides mid-single-digit growth, the leading players are able to drive double-digit organic profit growth through a coordinated set of actions to grow share and expand the market in their chosen sectors.

## Core TIC Growth Drivers – Profit Growth Potential

% CAGR

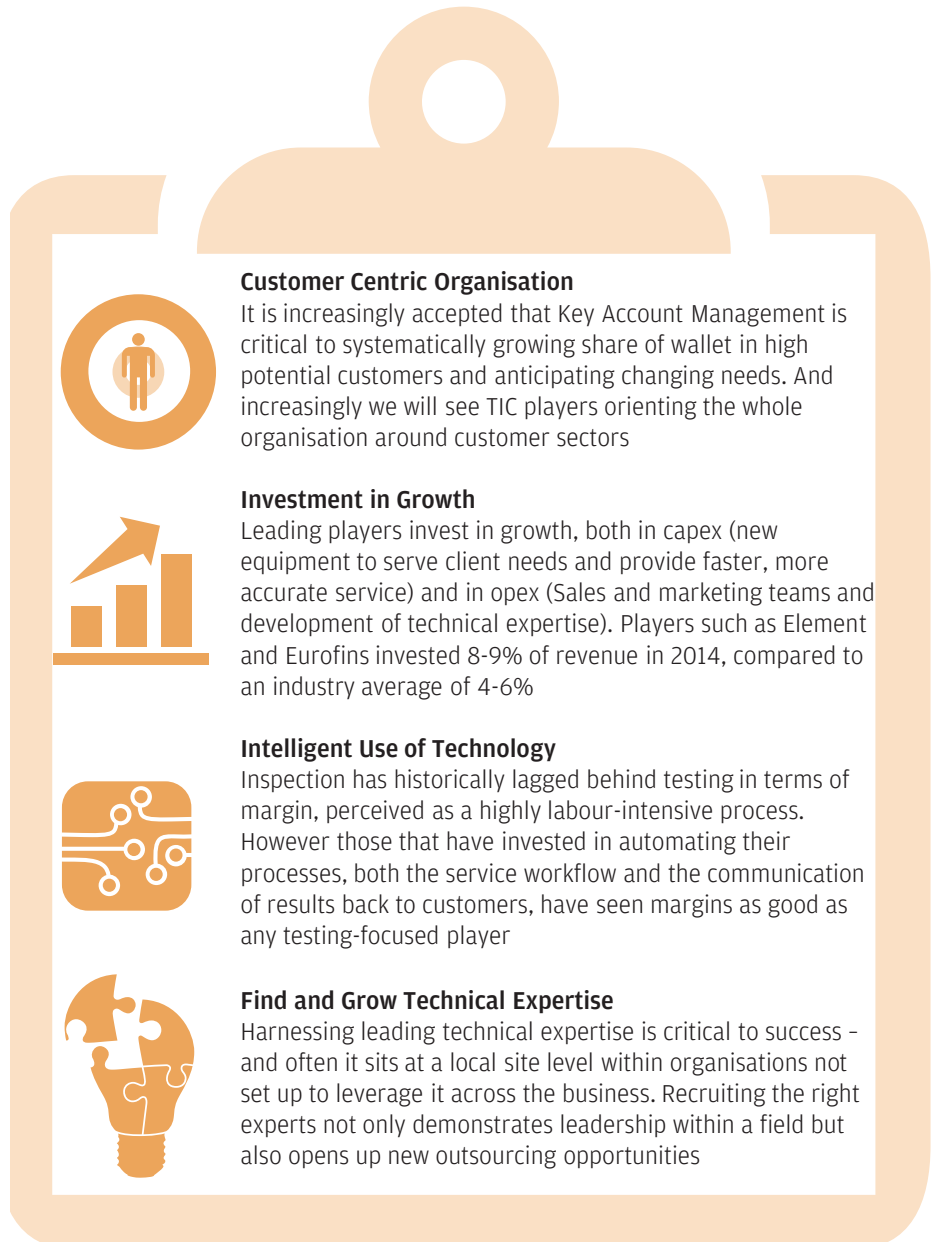



Accessing share of wallet growth and persuading customers to outsource is a hard task - and may require innovation and upskilling of business development capabilities. This is particularly so for companies who have not historically invested in organic growth and as a result are often internally focussed with limited change management capabilities. As such maximising the potential gains requires concerted effort.


M&A remains important, but increasingly as a route to drive organic growth, by offering an expanded range of capabilities to serve key customers - the multiples being demanded have moved this from a “nice to have” to a critical requirement for any acquisition (see Eurofins case study, right).

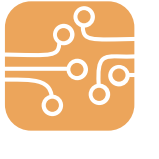
# A WINNING FORMULA?


Looking at the winners and losers in the Index, and from speaking with end-customers, we see a number of ways in which leading players can ensure they capitalise on a changing market environment:



- **Customer Centric Organisation**

It is increasingly accepted that Key Account Management is critical to systematically growing share of wallet in high potential customers and anticipating changing needs. And increasingly we will see TIC players orienting the whole organisation around customer sectors
- **Investment in Growth**

Leading players invest in growth, both in capex (new equipment to serve client needs and provide faster, more accurate service) and in opex (Sales and marketing teams and development of technical expertise). Players such as Element and Eurofins invested 8-9% of revenue in 2014, compared to an industry average of 4-6%
- **Intelligent Use of Technology**

Inspection has historically lagged behind testing in terms of margin, perceived as a highly labour-intensive process. However those that have invested in automating their processes, both the service workflow and the communication of results back to customers, have seen margins as good as any testing-focused player
- **Find and Grow Technical Expertise**

Harnessing leading technical expertise is critical to success – and often it sits at a local site level within organisations not set up to leverage it across the business. Recruiting the right experts not only demonstrates leadership within a field but also opens up new outsourcing opportunities

## CASE STUDY: EUROFINS

- Eurofins stands out in the market having achieved both strong M&A growth and strong organic growth.
- It has followed a strategically focussed acquisition policy over the last 10 years, investing only in its core markets (46 acquisitions since 2005)...
- ...but it has also made significant organic investments, including the creation of green-field sites and investment in start-ups (17 between 2006&10), both of which are rare in the industry, resulting in 7% average organic growth from 2010-14
- Eurofins have also invested in corporate resources to prepare for future size and to drive organic growth (+€26m central costs since 2005)
- This strategy has resulted in their outright leadership position in their core markets and very close customer relationships

# Offices

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For more information on OC&C's TIC 101 Index please contact

**Bennet Summers**

[bennet.summers@occstrategy.com](mailto:bennet.summers@occstrategy.com)

**Vivek Madan**

[vivek.madan@occstrategy.com](mailto:vivek.madan@occstrategy.com)