

Professional Services

The UK professional services industry has displayed resilience in the face of disruption caused by COVID-19, with various market segments showing steady growth prospects.

While COVID-19 proved a test for professional services firms, those that demonstrated resilience in adapting their services and business models to the rapidly changing market conditions are best positioned to attract buyers and investors moving forwards.



Overview

The professional services sector covers a diverse array of knowledge-intensive industries that provide specialised services to businesses. While there is undoubtedly overlap between sectors within the professional services ecosystem, there is notable variation across sectors. Each sector has been impacted by COVID-19 in contrasting ways, with different challenges and opportunities to consider as the economy emerges from the pandemic.

Two traditional professional service industries are covered in greater depth within this report: accounting and legal services.

M&A appetite for robust opportunities remains high. A survey of buyers and investors in professional services provided the following insights:



Market Structure

The scope of the industry is broad, covering industries such as legal services, accounting, advertising, architecture, scientific research and development, and management consulting. Although providing contrasting services, what defines these firms as professional services is their application of specialist knowledge to create customised solutions addressing client needs and problems.

Professional services firms operate in a dynamic and continually changing environment. The ability of firms to adapt to the changing demands of clients has been a key factor in driving growth. New services emerge to meet new market needs, creating growth opportunities for firms able to adapt to the market. Accounting firms have notably evolved to go beyond accountancy, audit, and tax, incorporating adjacent services such as M&A advisory, wealth management, and legal services in their offerings.

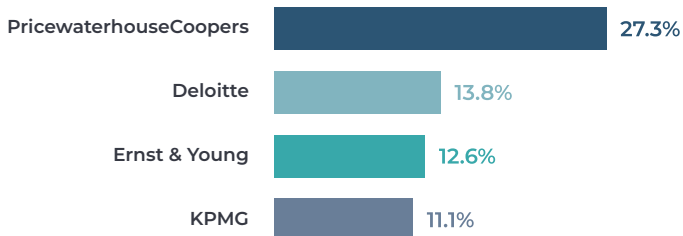
At all stages of growth, companies require commercial and advisory services from external accountants, consultants, and other specialists. With the impact of technological disruptions, globalisation, and uncertainty surrounding events such as Brexit, there will be increased demand for specialist advisors to guide businesses through new challenges and opportunities.

Accounting

The **UK accounting industry is estimated to be worth £5.3 billion**, having fallen at a compound annual growth rate of 0.9% between 2016 and 2021. This stems from economic disruption caused by COVID-19, which offset a growth period driven by strong levels of capital expenditure and M&A activity creating demand for accounting and auditing services.

Demand is expected to rise as the economy recovers from the pandemic. The accounting market is projected to grow at a compound annual growth rate of 2.9% to £6.1 billion by 2026.

The sector is dominated by the four largest players who collectively hold 64.8% of market share: PricewaterhouseCoopers (27.3%), Deloitte (13.8%), Ernst & Young (12.6%), and KPMG (11.1%).



Market share concentration is particularly prevalent at the upper end of the industry. These four firms audit 96% of the FTSE 350, as well as all of the UK's 100 largest firms.

Demand for accounting services is also sufficiently high at the mid-market level for firms to flourish, with increased demand from clients for mid-tier accounting firms to provide a greater breadth of professional services. The lower end of the market, on the other hand, is relatively saturated and competitive, with high quantities of firms targeting smaller businesses. These factors are expected to drive market consolidation and M&A activity as accounting firms seek to grow their customer bases and expand into new service lines such as management consulting and legal services.

Legal Services

The **UK legal services industry is estimated to be worth £35.2 billion**, having grown at a compound annual growth rate of 0.2% since 2016. While demand for transactional legal services has been significantly reduced by COVID-19, countercyclical practice areas such as litigation and insolvency have benefited from economic disruption, softening COVID-19's overall impact on the legal market.



Industry revenue is forecast to grow to £40.3bn in 2026 at a compound annual growth rate of 2.7%, driven by returning business sentiment and appetite for M&A post-COVID. Additionally, specialist legal advice is expected to be in demand as businesses attempt to adjust to the legal and regulatory landscape of a post-EU environment.

The industry has a low level of market share concentration. The top four firms account for just 6.6% of market share. Many legal service providers cater to a limited geographic area and are run as sole proprietorships or small partnerships. With such fragmentation, the industry is ripe for consolidation for firms looking to expand their practice areas and geographic reach through M&A. The largest law firms have also used M&A as a key growth method to acquire new practice capabilities or expand overseas.

Increased M&A activity and global expansion highlight the industry's maturity. Despite ongoing consolidation, the number of market players is expected to increase. In recent years, the legal services industry has opened to market entrants from other professional services industries due to legislation allowing non-lawyers to own law firms through alternative business structures. Legal service providers are likely to become attractive acquisition targets for professional services firms seeking entry into the legal market.

Industry Trends

Digital Transformation

A McKinsey & Co. study concluded that COVID-19 has, on average, accelerated digital transformation for businesses by seven years.

Technology and digital disruption have become key concerns for many professional services firms, especially as most have had to adapt to remote service provision. A 2021 survey of strategic and private equity buyers found the largest motivator of M&A for professional service firms was to acquire digital technologies and advisory capabilities enabling them to serve clients digitally or advise on these technologies.

A high-profile example of this is US professional services firm Jacobs Engineering Group's acquisition of UK innovation and transformation consulting firm PA Consulting. The partnership gives Jacobs access to digital consulting capabilities while enabling PA Consulting to enhance its services and achieve greater scale.

For many firms, an acquisition is the most efficient method of securing and scaling their digital capabilities. 54% of strategic acquirers within the professional services industry reported using M&A to broaden their digital service lines. While firms can invest in digital transformation organically, leveraging a pre-existing company's capabilities through a merger or acquisition allows for this process to be fast tracked, avoiding the significant time investment required.

Professional Services Convergence

Firms actively seeking to acquire digital capabilities and services from adjacent industries is reflective of ongoing convergence that is prevalent amongst larger professional services firms.

Take Ernst & Young (EY) as an example. The firm's acquisition of the Parthenon Group in 2014 enabled its expansion into strategy consulting. Acquiring Riverview Law in 2018 declared EY's intent to secure market share and disrupt the legal services market. An active M&A strategy has facilitated the company's expansion within other sectors, such as operations, HR, technology, and financial services consulting, as highlighted by the example acquisitions listed below.

EY Acquisition	Sector
Riverview Law	Legal Services
Parthenon Group	Strategy Consulting
Innovalue	Financial Services Consulting
Seren	Digital Consulting
PeopleFirm	HR Consulting

By enhancing the breadth of expertise and providing a more comprehensive set of services addressing client needs, service providers can cross-sell and ultimately build deeper strategic relationships with clients.

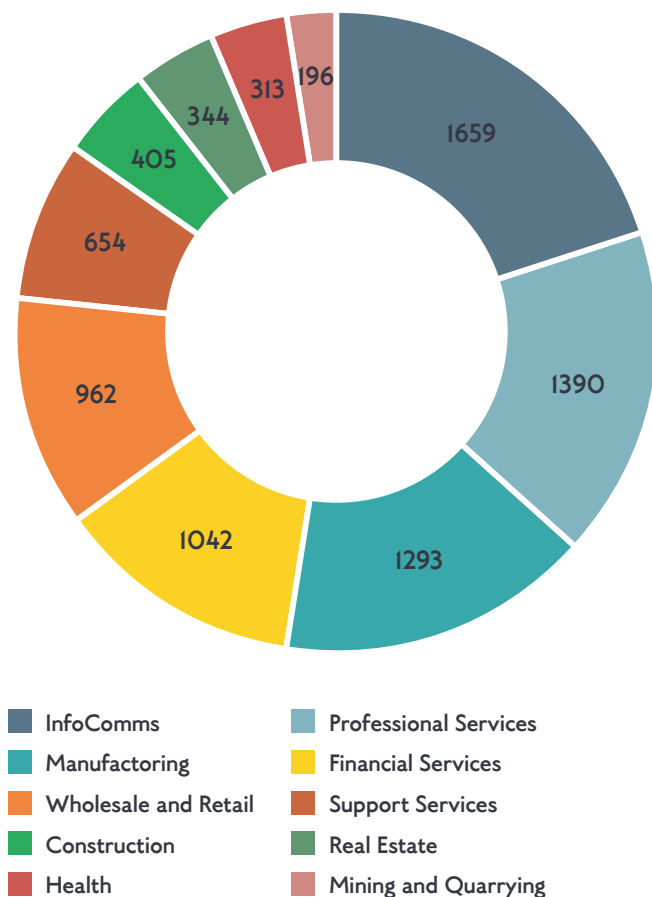


M&A Activity

An Active Market

While COVID-19 initially slowed down M&A activity in certain sectors, transaction volumes within professional services rapidly bounced back during 2020. The sector ranked second for volume of UK M&A transactions with 1,390 transactions in 2020, ahead of financial services, healthcare, and manufacturing.

Number of UK M&A Transactions by Sector (2020)



Private Equity Activity

With over \$1.9 trillion of dry powder held globally, private equity firms are expected to have considerable appetite for deal making but with higher expectations when evaluating investment opportunities. Like strategic buyers, professional services private equity investors have seen good opportunities in increasingly limited supply, with 73% reporting a fall in the number of attractive, available acquisition opportunities in 2020 due to COVID-19. Given the pandemic's widespread disruption, investors remain cautious when evaluating a company's financial performance during COVID-19 and how that will translate into the future as the world reopens.

Accounting M&A

Market analysis of M&A activity in the UK accounting sector reveals an active transactional environment, with over 40 deals completed since April 2020.

i. There is increased convergence amongst professional services sectors, with other types of professional services firms acquiring accounting capabilities through M&A:

Deal Date	Company	Buyer	Deal Size (£m)
11-Mar-21	David Rubin & Partners	Begbies Traynor Group	25.00
18-Jan-21	CVR Global	Begbies Traynor Group	Undisclosed
07-Sep-20	Fitzgerald & Law	Zedra (via Corsair Capital)	Undisclosed
01-Sep-20	Smith & Williamson	Tilney Group	1,836.48

ii. Acquisitions enable market players to grow geographically and scale into new UK regions:

Deal Date	Company	Buyer	Deal Size (£m)
01-Apr-21	Kench & Company	Ridgefield Consulting	Undisclosed
02-Oct-20	Bailey Group	SKS Business Services	Undisclosed
07-Sep-20	Fitzgerald & Law	Zedra (via Corsair Capital)	Undisclosed

iii. Accounting technology businesses, ranging from web-based payroll applications to multi-currency accounting software have attracted investment from venture capital and private equity investors:

Deal Date	Company	Investor	Deal Size (£m)
19-Feb-21	AccountsIQ	Finch Capital	5.10
01-Feb-21	Voly	Magenta Partners	Undisclosed
08-Jan-21	Staffology	IRIS Software Group (Via Intermediate Capital Group)	Undisclosed

Legal Services M&A

Market analysis of legal services M&A in the UK reveals a highly active transactional environment, with over 100 deals completed since April 2020.

i. There is considerable market consolidation amongst regional law firms using M&A for buy-and-build strategies to expand geographically:

Deal Date	Company	Buyer	Deal Size (£m)
22-Mar-21	Mundays	Knights plc	5.30
14-Dec-20	OTB Eveling	Knights plc	2.10
01-Dec-20	Glynis Wright & Co	Nelsons Solicitors	Undisclosed
24-Apr-20	Beaumont Legal	Metamorph Law	Undisclosed
24-Apr-20	Shulmans	Knights plc	20.00

ii. Firms from other professional services segments have started expanding into legal services via acquisitions:

Deal Date	Company	Buyer	Deal Size (£m)
29-Jan-21	KL Heritage	Deloitte	Undisclosed
29-Oct-20	Ellis Whittam	Marlowe	59.00

iii. Financial sponsors take interest in legal technology providers and legal consultancies, both as direct investments and bolt-on acquisitions for portfolio companies:

Deal Date	Company	Investor	Deal Size (£m)
05-Mar-21	Syke	Lawyers on Demand (via Bowmark Capital)	Undisclosed
05-Nov-20	Mason & Cook	BigHand (via Levine Leichtman Capital Partners)	Undisclosed
19-Jun-20	Eclipse Legal Systems	The Access Group (via TA Associates Management and HG Capital)	56.50

Threats to the Sector

Increased Competition

One of the key threats faced by professional services firms is increased competition. This competition comes from both the largest professional services providers expanding horizontally into adjacent markets, as well as new market entrants. In a survey of large law firms in the UK and US, 23% reported having lost mandates to the Big Four accounting firms, which they would have normally expected to win. Similarly, a study found that 20% of management consulting work goes to independent freelance consultants.

Brexit

The post-Brexit status of service professionals was not comprehensively addressed during trade deal negotiations, which has created significant uncertainty. Visas and work permits, with rules unique to each country, have encumbered service provision within the EU. For example, British-qualified accountants no longer have a credential automatically recognise by all

EU member states. Certain EU member states such as Germany, Italy, and Spain still recognise UK professional accountancy qualifications without restrictions; however, certain EU countries such as France, Denmark and Greece now require British accountants to undertake an 'economic needs' test to work in or with their respective country. These restrictions present potential barriers to cross border business.

Technology: Automation and AI

New technological developments such as automation technologies and artificial intelligence have significant potential to change and reimagine how clients are served within professional services.

While statistics around automation and AI taking over manual jobs in professional services provide a pessimistic framing for the future of the industry, automation technologies and AI can also represent an opportunity. Having routine tasks automated by technology frees up time for strategic initiatives and advisory work where greater value can be provided to clients. Rather than replacing professional services functions, disruptive technologies are expected to change the types of skills and jobs required, ultimately increasing efficiency and quality of client service for firms willing to adapt.

Outlook

Growth in the UK professional services industry has been above average, with annual growth of gross value added between 2000 and 2020 exceeding that across the UK economy by approximately three percentage points. In 2020, professional services market revenue was £399 billion. Future growth is expected to be in line with the global professional services market, which

is projected to grow to \$6.5 trillion in 2023 at a 4.78% compound annual growth rate.

Uncertainty surrounding how professional services firms will operate in the EU's post-Brexit environment has the potential to constrain growth for international firms serving EU-based clients. This will become clearer over time. Various professional services sectors, including accounting, tax, and legal services will be essential for helping businesses navigate the uncertainty created by Brexit, as well as new opportunities that arise.

The professional services industry is constantly evolving, driven by client needs. The sector adapted well during COVID-19; however, firms will need to continue adapting as client needs evolve. Ongoing widespread digital transformation presents both opportunities and challenges for the industry.

M&A activity within professional services is expected to increase, driven by firms wanting to acquire new service capabilities or expand geographically. The accounting and legal services sectors are at a mature stage of their lifecycle, with steady growth expected as the UK looks towards life post-COVID. A wave of consolidation is anticipated across the industry, with larger players acquiring smaller players and smaller players using acquisitions to scale.

Gerald Edelman services

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