THE POTENTIAL INFLUENCE OF INSTITUTIONAL INVESTORS ON CONSTRUCTION ORGANISATIONS.

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A small number of investment companies seem to be on the verge of prescribing the future direction of management philosophy in the UK construction industry. Prominent industrial figures have called for the industry to embrace radical change. Egan in his "Rethinking Construction" Report personifies client power, however a more cogent force is the institutional shareholders who epitomise investor power. The strength of the major shareholders is perhaps far greater than any other stakeholder in the industry. This paper considers the inter-relationships of the major shareholders in the UK construction industry with particular reference to the leading 20 contractors and materials suppliers.

Detailed analysis of significant cross-border holdings found within the construction organisations major shareholders indicates the impact of such holdings and the influence upon strategic management perspectives.

The nature of shareholder investment patterns suggests that changes brought about will lead to a paradigm shift in construction management philosophy and practice. Shareholder tactics may surpass single organisational survival as the underlying strategic objective, i.e. shareholders maximising the return from their investment.

Keywords: shareholder, cross border holding, financial institution, change management.

INTRODUCTION

Construction works form an important part of the assets of the United Kingdom. Yet there has been minimal research into the ownership of the largest organisations within the industry, who tend to be Public Limited Companies (plc).

Sommerville (1993) highlighted the move to invest in, and agglomerate, contracting organisations, whilst Keynote (1994) market research report, highlighted the tendency of financial institutions to invest in the shares of the large construction companies. More recently an article in Building, (King ,1999) highlighted the holdings that Phillips and Drew Fund Management (PDFM) have in the construction industry and alluded to the complicated matrix of such holdings.

The inter-relationships and cross-border holdings that exist between the leading construction organisations, their corporate advisers and the major shareholders are of interest to the wider construction community and this paper highlights the extent and nature of these institutional investors' holdings. It is envisaged that the power, which is inherent in these sizeable stakes, may allow the City institutions to dictate the precise nature and scope of change in the UK construction industry, unless the industry itself can successfully manage the shareholders.

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THE UK CONSTRUCTION INDUSTRY'S PERFORMANCE

Various reports and studies undertaken in the last four decades, for example, Banwell (1964), Latham (1994), The Technology Foresight Report (Young, 1995), Egan (1998) and Love and Li (1998), have all highlighted the construction industry's poor levels of performance in comparison with other industrial sectors.

Perhaps an explanation for the long-term failure to improve performance can be put down to the parties who have called for change. Traditionally the call has come from external sources, who possess little direct influence over the construction executives and their business strategy. However the present call for change emanates from the major shareholders, who own the leading construction organisations and therefore possess real influence in the construction board rooms. Effectively, the contemporary business agenda is set by the needs of the dividend hungry shareholders (Knutt, 1998).

Mediocre performance will not be tolerated (King, 1999), and therefore it is the fund managers, financial institutions and banks i.e. The City, by means of their majority shareholdings that drive change.

MAJOR CONSTRUCTION SHAREHOLDERS

In order to establish what the extent of influence is, it is necessary to define the underlying shareholdings and by implication, the extent of control. Research has highlighted five major shareholders in the UK construction industry, namely, Prudential Plc, Union Bank of Switzerland (UBS), Schroders Plc, Merrill Lynch & Co Inc and Commerzbank AG.

Prudential Plc

Prudential may be held to be the major shareholder in the UK construction industry. Table 1 indicates an alphabetical list of the construction organisations that the Prudential and its subsidiary organisations such as Prudential Portfolio Managers (PPM) (Dun and Bradstreet, 1999) have in the UK construction industry. PPM manages £145Billion world-wide mostly on behalf of Prudential's internal clients and PPM Property is the UK's largest property investor with a portfolio valued in excess of £9 Billion (Prudential, 1999). The breadth of Prudential's holdings and the size of each stake provides them with a formidable array with which to direct how the industry operates.

UBS

UBS is the foremost bank in Switzerland and amongst their subsidiary organisations are Philips and Drew Fund Management (PDFM), UBS UK Holdings Ltd. Graham & Whiteside, 1999). It is through these two organisations that UBS invests in the UK construction industry, and the pattern is indicated in Table 2.

Schroders plc

Schroders is a leading international investment banking and asset management group. Table 3 denotes the construction organisations where Schroders possess a majority shareholding.

Table 1: Prudential's Shareholding in the UK Construction Industry.

Company	**Holding (%)**	**Company**	**Holding (%)**
Aggregate Industries	14.95	Keller Group plc	7.00
AMEC plc	5.90	Lavendon Group plc	17.25
Anglian Group plc	8.22	Marshalls plc	5.82
Ashtead Group plc	7.42	McAlpine (Alfred) plc	5.51
Atkins (WS) plc	6.14	Meyer International plc	3.10
Bellway plc	8.07	Mitie Group plc	3.45
Berkeley Group (The) plc	5.17	Mowlem (John) & Co Plc	4.35
BICC plc	9.94	Persimmon plc	13.08
Blue Circle Industries plc	3.49	Pilkington's Tiles Group plc	5.11
Bovis Construction	10.75	Redrow Group plc	4.10
Bovis Homes Group Plc	3.46	RMC Group plc	4.97
BPB Plc	8.00	Ruberoid plc	6.90
Bryant Group Plc	5.85	Rugby Group plc (The)	5.72
Caradon plc	6.06	Sharpe and Fisher plc	8.59
Crest Nicholson plc	4.95	SIG plc	5.97
Eve Group plc	22.87	Swan Hill Group plc	3.34
Fariview Holdings plc	7.11	Taylor Woodrow plc	5.04
Galliford	7.98	The Rugby Group plc	5.72
Gleeson (MJ) Group plc	6.23	Tilbury Douglas plc	14.33
Glynwed International plc	5.88	Titon Holdings plc	7.94
Graham Group plc	6.10	Travis Perkins plc	5.94
Halstead (James) Group plc	4.38	Wates City of London Properties Plc	7.78
Havelock Europa plc	22.87	Westbury Plc	14.47
Hepworth plc	3.80	Wilson Bowden plc	3.47
Heywood Wiliams Group plc	6.17	Wimpey (George) plc	15.00
IMI Plc	3.58	Wolseley plc	3.64
Jarvis Plc	5.90		

Source Hemmington Scott Web Site (http://www.hemscott.co.uk/).

Table 2: UBS's Shareholding in the UK Construction Industry.

Company	**Holding (%)**	**Company**	**Holding (%)**
Ashtead Group plc	3.31	IMI plc	5.86
Babcock International Group plc	20.72	John Mansfield Group plc	8.04
BICC plc	4.53	McAlpine (Alfred) plc	12.27
Bovis Construction	10.75	Meyer International plc	7.34
Cape plc	4.08	Mowlem (John) & Co Plc	17.83
Carillion plc	17.59	Norcros plc	13.08
Countryside Properties plc	4.88	Ruberoid plc	12.01
Darby Group plc	17.94	Swan Hill Group plc	17.41
Dyson (J&J) Plc	6.32	Tarmac plc	18.14
Fariview Holdings plc	10.90	Tay Homes	11.57
George Wimpey	12.92	Try Group plc	24.97
Gibbs and Dandy plc	14.36(A)	Wates City of London Properties Plc	4.05
Graham Group plc	11.47	Westbury Plc	5.10
Hepworth plc	12.98	Wilson Connolly Holdings plc	11.00

Source Hemmington Scott Web Site (http://www.hemscott.co.uk/).

Merrill Lynch & Co Inc

Merrill Lynch is a prominent financial management and advisory company and through Mercury Asset Management they hold shares in the construction firms outlined in Table 4.

Commerzbank AG.

Commerzbank own 97.2% of Jupiter International Group plc (Commerzbank, 1999). Who in turn are the parent company of Jupiter Asset Management (JAM) (Dun &

Bradstreet, 1999). Table 5 highlights the construction organisations where JAM have a major shareholding.

Table 3: Schroders' Shareholding in the UK Construction Industry.

Company	Holding (%)	Company	Holding (%)
AMEC plc	13.1	Flare Group plc	19.29
Amey plc	12.17	Graham Group plc	17.17
Ashtead Group plc	7.08	Johnston Group plc	5.96
Bellway plc	10.01	Keller Group plc	17.07
BICC plc	13.03	Lilleshall plc	10.21
Bovis Construction	5.85	Pilkington's Tiles Group plc	19.28
Cape plc	18.43	RMC Group plc	11.97
Crest Nicholson plc	19.35	Swan Hill Group plc	19.59
Ennstone plc	3.01	Taylor Woodrow plc	10.93
Eve Group plc	19.98	Utilitec plc	19.05

Source Hemmington Scott Web Site (http://www.hemscott.co.uk/).

Table 4: Merrill Lynch's Shareholding in the UK Construction Industry.

Company	Holding (%)	Company	Holding (%)
Bovis Construction	4.06	Meyer International plc	4.03
Carillion plc	10.67	Morgan Sindall plc	4.84
Countryside Properties plc	14.06	Norcros plc	3.06
Flare Group plc	8.00	Persimmon plc	5.87
Graham Group plc	5.67	RMC Group plc	15.99
Hewden-Stuart plc	5.76	Swan Hill Group plc	4.36
Johnston Group plc	5.06	Travis Perkins plc	3.20
McInerney Holdings plc	8.17	Wiggins Group plc	3.79

Source Hemmington Scott Web Site (*http://hemscott.co.uk/).*

Table 5: Commerzbank's Shareholding in the UK Construction Industry.

Company	Holding (%)
Abbey Plc	5.06
Babcock International Group plc	9.7
Baldwins Industrial Services plc	8.1
Cussins Property Group plc	13.44
Fairbriar plc	5.36
Fariview Holdings plc	8.76
Interior Services Group plc	9.77
Jarvis Plc	10.38
Linden plc	8.1
McAlpine (Alfred) plc	5.43
McInerney Holdings plc	5.65
Morgan Sindall plc	4.93
Persimmon plc	5.28
Utilitec plc	6.88

Source Hemmington Scott Web Site (*http://hemscott.co.uk/).*

CROSS –BORDER HOLDINGS OF THE MAJOR SHAREHOLDERS

Table 6 indicates the cross-border holdings that the major shareholders possess in the twenty largest materials suppliers and contractors. In some instances their combined holding is considerable, for example they held just over 40% of the Graham Group (Hemmington Scott, 1999A), who were taken over by Meyer International (where they had a joint holding of 14.47%) who now find themselves the subject of a take-over by Saint Gobain. The joint investors group hold almost a third of RMC, and they held 31% of Bovis, by means of their stake in P & O, although Bovis have been sold off to Australian Developers Lend Lease as P & O concentrate on core activities. The joint holdings serve to further highlight the combined strength of these organisations in the construction sector.

Table 6: Joint Shareholdings in Top 20 Contractors and Materials Suppliers.

	Major Shareholders and % holding					
Company	**Prudential**	**UBS**	**Schroder**	**Merrill Lynch**	**Commerzbank**	**Total %**
Bovis	10.75	10.75	5.85	4.06	0	31.41
Balfour Beatty	9.94	4.53	13.03	0	0	27.50
Carillion	0	17.59	0	10.67	0	28.26
Mowlem	4.35	17.83	0	0	0	22.18
Wimpey	15.0	12.92	0	0	0	27.92
Taylor Woodrow	5.04	0	10.93	0	0	15.97
McAlpine	5.51	12.27	0	0	5.43	23.21
Jarvis	5.9	0	0	0	10.38	16.28
Persimmon	13.08	0	0	5.87	5.28	24.23
Babcock International	0	20.72	0	0	9.7	30.42
RMC	4.97	0	11.97	15.99	0	32.93
IMI	3.58	5.86	0	0	0	9.44
Meyer International	3.1	7.34	0	4.03	0	14.47
Travis Perkins	5.94	0	0	3.2	0	9.14
Hepworth	3.8	12.98	0	0	0	16.78
Graham Group	6.1	11.47	17.17	5.67	0	40.41

Source Hemmington Scott Web Site (*http://hemscott.co.uk/).*

MAJOR SHAREHOLDERS AND THEIR INTER-RELATIONSHIPS

The major shareholders would appear to be separate entities with no clear links. However this is not the case, as the cross-border shareholdings of the major shareholders extend to each other as well as to the leading players in the construction industry (Hemmington Scott, 1999A). Schroders are the only major shareholder in Prudential, with a stake of 4.67% and in turn, Prudential have a 3.34% shareholding in Schroders. Furthermore, Warburg Dillon Read, who are a subsidiary of UBS, another major construction shareholder, are both brokers and financial advisers to the Prudential (Graham and Whiteside, 1999). Which illustrates the rather circuitous relationships which exists between the leading shareholders in the construction industry.

Comparative Financial Strength of Construction Organisations and Shareholders

A key measure used by the City to assess an organisation’s financial acumen is market capitalisation. Market capitalisation is a product of the number of shares in a company and the value of the traded shares. A high market capitalisation suggests a firm can raise cash for projects or acquisitions by issuing shares. Table 7 illustrates the market capitalisation of the Top 20 UK contractors and materials firms of 1999.

On an industry comparison, the difference in market capitalisation is evident. The top ranked materials supplier by market capitalisation is CRH, (£4.3Billion), which is in excess of the combined market capitalisation of Berkeley, Barratt, Taylor Woodrow, Amec, Kvaerner, George Wimpey, Beazer and Persimmon (£4.2Billion), who are the top eight contractors when ranked by market capitalisation.

The gulf is further increased however, when the market capitalisation of the major shareholders is considered. The current market capitalisation of Prudential Corporation Plc is in excess of £18 Billion (London Stock Exchange, 1999) and points to their standing as a Blue Chip stock. Whilst UBS is one of the world’s top 5 banks by market capitalisation and whose draft figures are on a par with the Prudential (UBS, 1999).

Table 7: Market Capitalisation of Top 20 UK Contractors and Materials firms (1999)

Contractors			**Materials**		
Rank by Turnover	**Organisation**	**Market Capitalisation (£m)**	**Rank by Turnover**	**Organisation**	**Market Capitalisation (£m)**
1	Kvaerner	491.88	1	Wolseley	2,419.13
2	Amec	521.29	2	RMC Group	2,447.58
3	Bovis	not available	3	CRH	4,394.39
4	Balfour Beatty	not available	4	Pilkington	1,118.93
5	Carillion	255.84	5	Blue Circle	2,880.04
6	John Mowlem	205.31	6	Hanson	3,051.12
7	John Laing	303.88	7	IMI	978.67
8	George Wimpey	468.28	8	BPB	1761.24
9	Taylor Woodrow	587.03	9	Tarmac	891.36
10	Barrat	611.79	10	Caradon	712.49
11	HBG	not available	11	Meyer Int	831.37
12	Kier	95.90	12	Rugby	612.19
13	Alfred McAlpine	283.43	13	Glynwed Int	542.87
14	Tilbury Douglas	313.11	14	Aggregate Ind	832.48
15	Beazer	405.92	15	SIG	267.12
16	Jarvis	374.66	16	Heywood Wiliams	197.18
17	Berkeley	742.25	17	Marley	not available
18	Bryant	365.36	18	Travis Perkins	682.68
19	Persimmon	398.05	19	Hepworth	507.38
20	Babcock Int.	176.97	20	Graham Group	247.41
Sum (market capitalisation)		6,600.95	Sum (market capitalisation)		25,375.63

Source: *London Stock Exchange web site (http://www.stockex.co.uk).*

Whereas the capitalisation of Amec (£521 Million) and CRH (£4.3 Billion), the largest in the contractors and materials suppliers sector, lag way behind that of Prudential and UBS. Furthermore, the combined market capitalisation of Schroders, Prudential, Merryl Lynch, UBS and Commerzbank is almost £65 Billion. The combined market capitalisation of the Top 20 contractors and materials suppliers is only £32 Billion.

The complex inter-relationships which exist in the construction supply chain, between the shareholders, the major players in the construction industry and the corporate advisers mean that the City institutions have the potential to direct the strategic direction of the UK construction industry.

Influence of the Financial Institutions

PDFM (part of UBS) were one of the prime drivers in the Tarmac and Carillion de-merger. The same fund managers were also behind the audacious but unsuccessful take-over bid for Marley by Mansfield, who were twice Mansfield's size. PDFM backed the bid because the objective was to replace the entire Marley management team (King, 1999). Changing some aspect of the existing organisation being a key driver that appears repeatedly.

Cronin and Barry (1999) highlight Taylor Woodrow's move from traditional high-risk contracting towards more fee-based work, property development and low risk projects, with the loss of 250 jobs. A spokesman for Taylor Woodrow emphasised the "good sense" of demonstrating to major shareholders that construction, whilst still a part of the groups activities represents a much reduced risk. However it seems the strategic change allied to job losses was not enough to reassure the City.

Morby (2000), reports that Taylor Woodrow intends to shed further staff from its contracting division as well as reducing turnover. Merrill Lynch (MAM) see the need for ‘major surgery’ at Taylor Woodrow Construction, whilst other analysts argue that the construction division should be able to turnover a sum of £400 Million with only 400 staff. The Group’s stated plan is to concentrate the streamlined construction division’s efforts on higher margin PFI projects, negotiated contracts and Facilities Management (FM). The emphasis being on a clear strategy shift that will produce increased returns from the resources employed.

Laing (1999) are also moving away from their traditional activities as they redefine their business plan. Their objectives include a concentration on profit as against turnover, with turnover reducing by about a third to £850 Million, with a reduction in staff of about 850. Moreover they are seeking to manage risk more effectively and to extend the range of services offered to clients

Alfred McAlpine are on the lookout for potential partners (Rogers, 2000) in an attempt to win recognition by the City. They aim to achieve this by means of consolidation, private housing work would be increasingly built off-site, with a knock on effect on traditional jobs. The intention being to de-skill and de-man the house building process.

Change is also afoot in the materials sector, and according to Smith (1999) two themes have emerged, consolidation and cost-cutting. For example, CRH staged a take-over of Ibstock, the UK’s second largest brick manufacturer. Whilst, Pilkington achieved savings of £200 Million by a programme of cost reduction and redundancies. The Graham Group were bought out by Meyer International who themselves are fighting a bid from Saint Gobain. Another French Group, Lafarge bought Redland (once a member of the FTSE 100 index) and attempted to gain control of Blue Circle.

The analysis suggests that the institutional investors are demanding performance improvements and are becoming increasingly proactive with organisations that fail to meet their requirements. Numerous companies in the contracting and materials sectors are finding out at first hand that their strategic management philosophy must change.

THE STRATEGIC IMPACT OF INSTITUTIONAL INVESTORS’ REQUIREMENTS

Clearly a number of construction firms are realigning their strategies in answer to the demands of the major shareholders. Some common themes to emerge from review of the material available: namely, takeovers/consolidation, de-mergers, downsizing, cost cutting and horizontal diversification.

De-mergers could see organisations jettison poorly performing, divisions, as they seek out a more profitable future, where competition is less fierce, margins are higher and the degree of risk is more acceptable. Concentration of effort and resources on a core business may be used as firms seek to find niche markets or specific areas of specialisation.

Take-overs and consolidation in the construction market place is another possibility and can either be friendly or hostile. The investors who are continually disappointed in an organisations performance may back any bid as they are desperate to dispose of their shares and will grasp at any reasonable cash offer. The offer may not necessarily be in the best interests of the organisation, but could be accepted as it provides a profitable escape route for the investors.

The figures quoted for Taylor Woodrow Construction (£1Million turnover for every member of staff) if applied as a benchmark measure across all contractors would have a significant effect on the employment characteristics of the industry.

Cost cutting could see flatter organisational structures, an increase in the span of control, an increase in stress, working hours and more emphasis put on the mobility of all construction personnel. Increased expenditure on training would be required so that the streamlined organisation could be effective. Streamlining the construction supply chain would be required, with a concentration on slimmed down number of suppliers in long term partnership arrangements. This allied to advances in communications technology would allow a company to greatly reduce overheads by running a business from a central head office.

Increased diversification into new areas such as Facilities Management and Consultancy work, where margins are higher and risk is reduced could also be introduced. Care would have to be taken, because if these new markets are flooded by new organisations then supply could easily outstrip demand. Consequently income may fall dramatically as too many organisations compete for too little work, especially if price is the main competitive factor.

If such alterations were implemented on a pan industry base there would be a wholesale shift in construction management theory and practice, and the UK industry would be markedly different in terms of nature, structure and culture. The overall shape of the industry could change, with an increase in the polarisation of contracting organisations. In effect the large contractors may, through mergers or acquisitions become global players or "Super Contractors" as the economies of scale that can be derived from size can be alluring. Whilst the lesser players are left to seek out niche markets to facilitate their survival. Likewise consolidation in the materials sector could mean the control of this important sector moves outwith the confines of the United Kingdom. Effectively the UK materials suppliers may become depots, as management jobs and strategy are centred elsewhere on the globe.

The Philip Holzmann saga has highlighted the possible implications of the complex inter-relationships between shareholders and corporate advisers. Deutsche Bank, Holzmann's biggest creditor as well as being the second largest shareholder, with a 15% holding, accused Commerzbank of inflexibility during the protracted negotiations (Tooher, 1999). Holzmann found that co-operation and help was not readily accessible, as the interested parties appeared to be working to differing agenda's.

Methodology for Testing the Strength of the Linkages

Given that the institutional investor are capable of being tracked, it is appropriate to then question them as to their intent, strategies, and impact awareness. The intention is to do so through a future research questionnaire that focuses upon these three areas and feeds into a briefing document which helps to shape management responses.

CONCLUSIONS

There is no doubting the institutional investors have the wherewithal to influence the future direction of the UK construction industry. They are becoming more vociferous in their actions as they attempt to boost the returns from their construction investments, because all too often profit has been wantonly neglected by construction organisations.

There are two broad approaches to the question of satisfying shareholders needs. The first involves a proactive long-term strategy, where the construction executives attempt to effectively manage shareholders needs. The other is reactive in nature, and involves senior managers merely reacting to shareholder wrath with short-term crisis management solutions. If the industry relies on the latter strategy, then change will occur which is shareholder led, driven and focused. There is no doubt the senior managers who adopt such a reactive strategy leave themselves open to the vicissitudes of the institutional investors. However if the industry attempts to integrate the needs of the shareholders with those of the shareholders then change will take place on the industry's terms.

A period of change is upon the industry, however it is unclear as to the extent to which the industry will change. The industry may see a raft of mergers/acquisitions, downsizing and cost cutting exercises, or control of major organisations moving abroad, all at the behest of the institutional investors. This may be agreeable to the shareholders but may not necessarily be in the best interests of the industry and the wider grouping of stakeholders.

The plight of Philip Holzmann serves as a timely reminder about what could happen in an economic down turn, especially where a few investors hold cross-border holdings. The shareholders interests come first, whilst, the needs of contractors, sub-contractors, suppliers, clients and employees come a distant second.

This paper has demonstrated the complex inter-relationships, which tend towards centralisation of the shareholders, bankers, brokers and financial advisers to the large construction organisations in the UK. These links suggest there is the possibility of a scenario developing, especially in a period of recession and if a protracted period of infighting ensues, whereby the institutional investors will lose sight of the industry, concentrating on protecting their own self interests.

Senior managers within the industry must take control of the situation and initiate a step improvement approach to the commitment and integration of profit generation, shareholder satisfaction with long term industrial sustainable growth and prosperity. A proactive decision to change strategic orientation will pre-empt any concentrated effort from shareholders to force change. Failure to do so may mean that change will be orchestrated unilaterally by the institutional investors. The power of the shareholders represents a crucial challenge to the future of the UK construction industry.

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