

Human Capital Market Review Q4 2020



Following a year of significant uncertainty for the sector, this edition of Gambit's Human Capital market review reflects on what has transpired over the course of Q420 and considers the implications of the key trends, statistics and macroeconomic drivers that are in play as we enter 2021. Significant encouragement can be taken from both the transaction and public company valuation data detailed in this report, both of which have been supported by a positive underlying strength of the labour market and the demonstrable Covid-19 resilience that the Human Capital sector has evidenced in 2020. However, a further marginal decline was evident in deal volumes in Q420, as social restrictions were reintroduced in the latter part of the quarter.

With stability and growth returning to the share prices of listed recruiters, the defensive strategies observed in 2020 will shift towards the prioritisation of growth, with the M&A market earmarked to play a pivotal role in post-pandemic strategic initiatives in 2021. Moreover, the agreement of a free trade deal between the UK and the EU in Q420 averted a potentially disruptive no-deal. This will encourage international strategic acquirers who are set to revisit previous cross-border strategies, following the resolution of a key legacy issue. Having successfully navigated the challenges of 2020, we expect that Human Capital companies will seize the opportunities presented by a buoyant M&A market in 2021.

Q420 Summary

- EV/EBITDA valuations in the Gambit Human Capital Index rose for the third quarter in a row, nearly doubling from Q120 and now significantly exceed the levels seen pre-pandemic.
- UK deal volumes rose by 33% in Q420, driven by increased domestic activity from strategic acquirers that have been encouraged to undertake acquisitions by an increasingly positive economic and sectoral outlook.
- In line with a growing appetite for Executive Search services, refreshed management teams will look to achieve operational scaling through successful acquisitions and the disposal of non-core assets to drive renewed strategic focus in the next economic cycle.
- Given the positive trajectory in the share prices of listed recruiters, the defensive strategies observed in 2020 will shift towards the prioritisation of growth, with M&A set to play a pivotal role in strategic initiatives in 2021.
- Q420 saw a rise in IT, Executive Search and General Staffing sub-sector transactions, with increased digitisation, the evolution of the C-Suite and rising candidate availability driving respective deal volumes upwards.
- Succession strategies are crystallising and the funding market is well equipped to support Human Capital companies with such initiatives, with particular interest in undertaking a Management Buy Out increasing as ambitious leadership teams look to facilitate legacy owners' exit strategies.
- Anticipated changes to Capital Gains Tax ("CGT"), compounded by a shift in shareholder priorities as a result of Covid-19 will have expedited succession plans further, leading to value maximisation opportunities for sellers to benefit from tax relief and buyers to capitalise on a rise in available assets.
- As a direct result of the pandemic, Human Capital companies are now actively searching for acquisition targets, with assets operating in Covid-19 resilient sub-sectors offering significant value and protection against future downturns.
- Companies with well-capitalised balance sheets will continue to seize ad-hoc diversification opportunities by acquiring into sub-sectors with favourable hiring trends, thereby enhancing their medium to long term prospects through proactive, pre-emptive financial and strategic preparation.



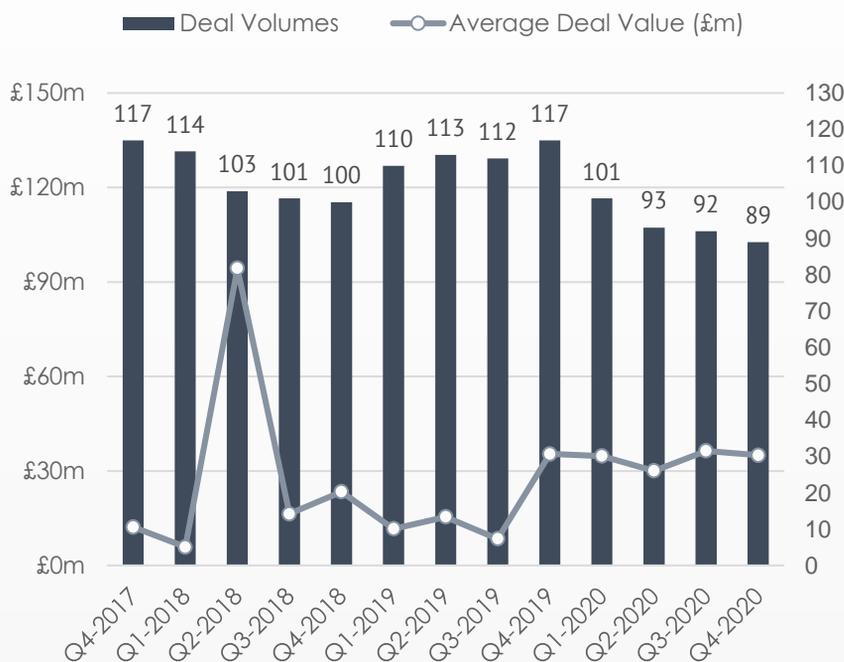
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“Human Capital companies will seize the opportunities presented by a buoyant M&A market in 2021”

Global M&A: Activity



Overview

- Despite a small drop in activity volumes, deal values continue to show consistency, indicative of the quality of assets and the level of optimism that exists around the sector's prospects in the short to medium term.
- UK deal volumes rose by 33% in Q420, driven by increased domestic activity from strategic acquirers, despite a reintroduction of lockdown measures in December.
- The Executive Search sub-sector saw significant appetite, with assets that have evidenced competency in facilitating the hiring of capable management teams that can deliver successful post-pandemic growth strategies becoming increasingly attractive.
- Deal volumes fell by 17% in 2020 when compared with 2019, in lockstep with SIA projections that the staffing sector would decline by 17% in 2020. However, 2021 is well poised to recoup this fall, with favourable sector fundamentals and SIA base case forecasts of 16% UK staffing sector growth in 2021.
- EV/EBITDA valuations in the Gambit Human Capital Index rose for the third quarter in a row, nearly doubling from Q120 and exceeding levels observed pre-pandemic.
- The sustained rise in our index reflects a growing awareness of the important role that Human Capital companies will play in the restaffing and retooling initiatives of post-pandemic economic activity.
- CPL Resources was acquired by Japanese recruiter Outsourcing for a consideration of €318m, a premium of more than 50% on its market capitalisation before the takeover bid was announced in November. The company will now be de-listed and will no longer feature in our index.
- Given the positive trajectory in the share prices of listed recruiters, the defensive strategies observed in 2020 will shift towards the prioritisation of growth, with M&A set to play a pivotal role in strategic initiatives in 2021.

Company Name	EV/EBITDA			
	Q1 2020	Q2 2020	Q3 2020	Q4 2020
Adecco S.A. (SWX)	6.3x	7.5x	9.7x	13.7x
Brunel International NV (ENXTAM)	10.3x	13.9x	15.3x	17.3x
CPL Resources PLC (LSE)	4.4x	5.4x	5.3x	8.7x
Empresaria Group PLC (AIM)	4.3x	4.5x	4.2x	4.4x
Gattaca PLC (AIM)	2.0x	2.3x	2.5x	0.9x
Hays PLC (LSE)	8.0x	9.3x	10.9x	14.2x
Impellam Group PLC (AIM)	8.1x	7.7x	5.8x	9.4x
ManpowerGroup Inc (NYSE)	4.8x	6.0x	7.4x	10.0x
Page Group PLC (LSE)	7.4x	7.9x	14.1x	16.9x
Prime People PLC (AIM)	1.7x	2.3x	1.7x	3.6x
Randstad Holding NV (ENXTAM)	7.5x	9.3x	12.4x	15.0x
Robert Half International Inc (NYSE)	6.6x	9.0x	9.7x	12.5x
Robert Walters PLC (LSE)	3.6x	5.0x	6.2x	7.7x
Staffline Group PLC (AIM)	4.1x	N/A	N/A	N/A
SThree PLC (LSE)	4.5x	5.5x	6.3x	7.6x
Gambit Human Capital Index	6.5x	8.0x	10.0x	13.1x

Public Company Valuation Trends



Key Points

- The graph above shows EV/EBITDA valuation multiples for the S&P Human Resources and Services Index over the last five years.
- Valuation data for Human Capital companies is highly responsive to signals of an economic 'return to normal', which often serve as a pre-cursor to sharp rebounds in the EV/EBITDA multiples, offering a clear barometer of activity for buyers and sellers.
- Analysis of the data suggests that valuation multiples have experienced a period of sharp appreciation in the second half of 2020, rebounding to beyond pre-pandemic levels in Q420 on the back of robust labour market fundamentals and an encouraging 2021 sectoral outlook.
- In line with the historical data, a period of valuation appreciation is a signal that the market is optimistic of the short to medium term prospects for growth, or it is indicative of a lack of organic opportunities to pursue.
- With the widely rumoured Capital Gains Tax changes set to be introduced in 2021, the data above presents a clear opportunity for sellers to engage with the M&A market during a period of valuation growth.
- Greater recognition of Human Capital companies' key role in leading economic recovery will also sustain valuations in the sector, with post-pandemic jobs growth firmly on the agenda of Chancellor Rishi Sunak in 2021.
- Deal makers have become adept at completing transactions in the current environment, with effective negotiation of Covid-19 adjustments paving the way for optimal value realisation opportunities.
- Proactive business owners should reach out to their advisory network to establish a best practice approach to maximise value realisation opportunities.

Sub-Sectors in Focus

IT



When compared with H120, IT sub-sector transactions rose by 70% in H220, in line with the trend of increasing digitisation. This is likely to endure, given the importance of robust IT infrastructures and technological innovations that ensure companies can continue to operate efficiently in years to come. To that end, employers are continuing to bolster capabilities by recruiting high quality talent with technological capabilities. Although the IT sector is one of the UK's fastest growing employers, there remains a shortage of candidate availability and this scarcity will ensure that sub-sector deal volumes and valuations will continue to be buoyant. Given IT recruiters' exposure to IR35, those that can demonstrate competency in navigating the April 2021 implementation will attract increased attention and further appetite from acquirers.

40% Growth in the number of jobs in UK technology companies in the last two years

Source: Tech Nation, Sept 2020

Executive Search



The stark rise in deal volumes in the Executive Search sub-sector reflects a growing impetus from forward thinking companies to reset company strategies and improve management teams for the post-pandemic environment. At a macro level, the pandemic has given C-Suite Executives the chance to reflect on the priorities and strategies that will secure the prospects of their respective businesses for the future. The rise also reflects the introduction of new C-Suite talent and titles into companies to address key issues such as sustainability, diversity and equality, creating significant demand for Executive Search recruitment services. We expect this positive trend to continue, increasing competition for quality assets with a legacy of success in meeting the evolving priorities of senior level strategic decision makers.

3% Of FTSE 100 Chairmen, CEOs and CFOs come from ethnic minority backgrounds

Source: The Times, January 2021

General Staffing



Against the backdrop of heightened candidate availability, General Staffing transactions rebounded in Q420. As is to be expected in the current economic environment, contract vacancies grew by 20% in the first week of December, with General Staffing recruiters benefitting from a 20% rise in hiring activity. Public and private sector emphasis continues to be placed on reskilling and retooling initiatives both domestically and internationally, with General Staffing recruiters set to play a pivotal role in post-pandemic recovery. In particular, cross border activity in the sub-sector rose four-fold, indicating that while companies in the sub-sector are not looking to diversify in a sectoral sense, they are doing so geographically, which will see increasing consolidation trends.

537k Amount of vacancies in the three months to November 2020, 20% higher than in the previous quarter

Source: ONS, Dec 2020

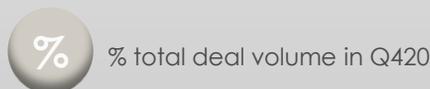
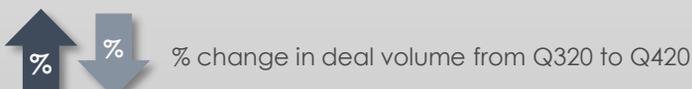
Engineering



A slight reduction in Engineering deal volumes occurred in Q420, however, a strong Q320 performance, drove a 10% H220 increase on H120, to conclude a resilient year of sub-sector activity. In the UK, the Engineering sub-sector is estimated by SIA to be the largest in the EMEA region. Recruiters servicing clients with national public sector contracts have been insulated from depressed demand and the UK's national infrastructure projects have priority in the domestic political and economic agenda. The STEM skills shortage in the UK is well-documented and employers continue to search for recruitment partners who can help increase their access to quality talent. These trends bode well for deal volumes and valuations in the sector in 2021.

£1.5bn The UK's STEM skills shortage costs businesses £1.5bn in additional training / retraining costs

Source: The Independent, July 2020



With 2021 poised to be a year in which Human Capital companies look to implement post-Covid-19 strategic plans, we set out below the most commonly cited strategies that businesses in the sector are prioritising and outline how M&A activity can catalyse and enhance these initiatives.

Growth

- As organic growth has become increasingly challenging, the M&A market's appeal has risen, offering Human Capital companies an effective means to achieve strategic goals.
- In line with the trend of growing interest in Executive Search recruiters and related hiring activity, refreshed management teams will look to achieve operational scaling through successful acquisitions and the disposal of non-core assets to drive renewed strategic focus in the next economic cycle.
- On the back of rising EV/EBITDA valuations, publicly listed Human Capital companies continue to build positions for growth and takeovers of undervalued companies, further enhancing their current positive growth trajectory and market ratings.

31% The level of growth in EV/EBITDA valuations of companies in the Gambit Human Capital index in Q420

Gambit Human Capital Index, Dec 2020

3 in 5 Human Capital companies stated that enhancing and transforming their technological capabilities is an area of specific focus

Gambit Human Capital Survey, Nov 2020

Digitisation

- While implementation of an effective digital strategy has long been discussed, it is now crucial to corporates' prospects in the sector, offering opportunities for geographic expansion with low physical outlay, increasing recruiters' market coverage.
- Lockdown measures have radically changed the addressable digital audience that recruiters have access to, therefore assets with a strong online presence offer ideal acquisition opportunities to technologically-inhibited recruiters.
- Larger Human Capital companies will continue to further their efforts to expand upon existing digitisation initiatives to insulate business models, driving a rise in the value of technology enabled assets in tandem.

Succession

- Anticipated changes to Capital Gains Tax ("CGT"), compounded by a shift in shareholder priorities as a result of Covid-19 has expedited succession plans, leading to value maximisation opportunities for sellers to benefit from tax relief and buyers to capitalise on a rise in available assets.
- The funding market is well equipped to support Human Capital companies with succession initiatives and Management Buy Out interest is rising as ambitious leadership teams look to facilitate legacy owners' exit plans.
- In view of potential succession issues, Human Capital business owners may increasingly look to sell to an Employee Owned Trust, which holds shares on behalf of the employees in the company, attracting no CGT.

60 The average age of shareholders exiting their business through undertaking a Management Buy Out

Gambit Exit Survey, Dec2020

22% Of surveyed staffing firms are now considering initiating a search for acquisition targets following the Covid-19 pandemic

SIA, Oct 2020

Diversification

- As a direct result of the pandemic, Human Capital companies are now actively searching for acquisition targets, with assets operating in Covid-19 resilient sub-sectors offering significant value for acquirers.
- Prepared companies that have prudently planned and well-capitalised balance sheets possess the capability to seize ad-hoc diversification opportunities by acquiring into sub-sectors with favourable hiring trends at short notice.
- Equally, Human Capital companies with larger portfolios may look to the sale of non-core, non-performing assets to provide additional capital to facilitate diversification into areas of strategic focus, driving overall M&A activity upwards.

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Gambit Corporate Finance

Established in 1992, Gambit is an independent corporate finance advisory firm specialising in advising private and public companies on mid-market transactions in the UK and overseas. With offices in London and Cardiff, Gambit is widely recognised as a market leader in M&A advice in the Human Capital sector having built up detailed industry knowledge and an enviable track record in deal origination and execution.

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