M&A Market Review
Human Capital
Q4 2018

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Contents

Contents	Page
Executive Summary	3
Human Capital – M&A Activity Analysis	4
Human Capital Regional M&A Activity	5
Human Capital Sub-sector Trends	6
Human Capital Public Comparables	7

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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Corporate Finance International

Gambit is the exclusive UK shareholder of CFI, a global partnership of middle-market investment banks and corporate finance advisory firms. With over 200 professionals located in 26 offices throughout the world. CFI members specialise in cross-border acquisitions, disposals, capital raising, and related services.

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Executive Summary

In Summary

- The volume of global human capital transactions remained flat in Q418, due to economic headwinds and a shortage of quality assets available
- European transaction volumes declined slightly but were still at a higher level than across the rest of 2018, due to a reduction in cross-border activity. However, conditions in domestic markets generally remain conductive to M&A activity and we expect to see higher deal volumes once certainty around Brexit is delivered
- There was a marked rise in transactions in the Middle East & Asia region, driven by increased consolidation by Japanese corporates
- UK unemployment remained at historic lows during Q418, and has not been lower since February 1975. Record employment coupled with increasing demand for staff in the UK means that the outlook for the sector is increasingly positive in the near term
- Whilst cross-border activity from Europe into the UK declined in Q418, the UK market continues to attract inbound investment from both the North American and Asian markets
- A shortage of skilled and qualified candidates in several sectors including IT and engineering is a concern and will likely drive strategic acquirers to pursue defensive M&A strategies, to ensure continuity of service offering and access to high quality candidate pools
- The Gambit HC index shows that valuations for public interest companies fell by 15% in Q418, this was due to the underperformance of global stock markets and reflecting ongoing economic and political uncertainty
- Once conditions stabilise we anticipate public interest companies taking advantage of the low cost of capital and assuaging pressure from shareholders to address recent share price erosion, by making earnings and value enhancing acquisitions

M&A Market Review
Human Capital
Q4 2018

Geraint Rowe
Partner, Human Capital

Global deal volumes declined slightly in Q418, driven by a fall in the number of cross-border transactions, however, confidence remains in the human capital market evidenced by a marked increase in investment from financial acquirers and active domestic markets. Activity declined by 11.8% in 2018, given the political backdrop to the year this is unsurprising as many in the sector have taken a "wait and see" approach to the market. The European market remains the most active but continues to be impacted by Brexit uncertainty, though with time running out until the UK leaves the EU it is likely that clarity will be delivered in the short term. Whilst deal activity has stalled, particularly amongst large corporates, we expect this to unwind once clarity is achieved. Several key economies are struggling with a lack of candidate availability and as a result many are now considering defensive M&A to ensure service offering and market share don't decline in key sectors. A continuing shortage of sellers in several key sectors such as IT and Engineering are increasing competition between strategic and financial acquirers driving valuations on private company deals upwards. Those with access to high quality staffing candidate pools and considering succession should consider interest from both strategic and financial purchasers. The performance of public interest companies in the Human Capital sector in Q418 was disappointing, but was caused by stock markets declining globally. Organic growth in many sectors is likely to be insufficient to boost market ratings and with the cost of capital remaining low, it is likely that public interest companies will look towards earnings enhancing M&A in an effort to pacify shareholders unhappy with recent share price erosion

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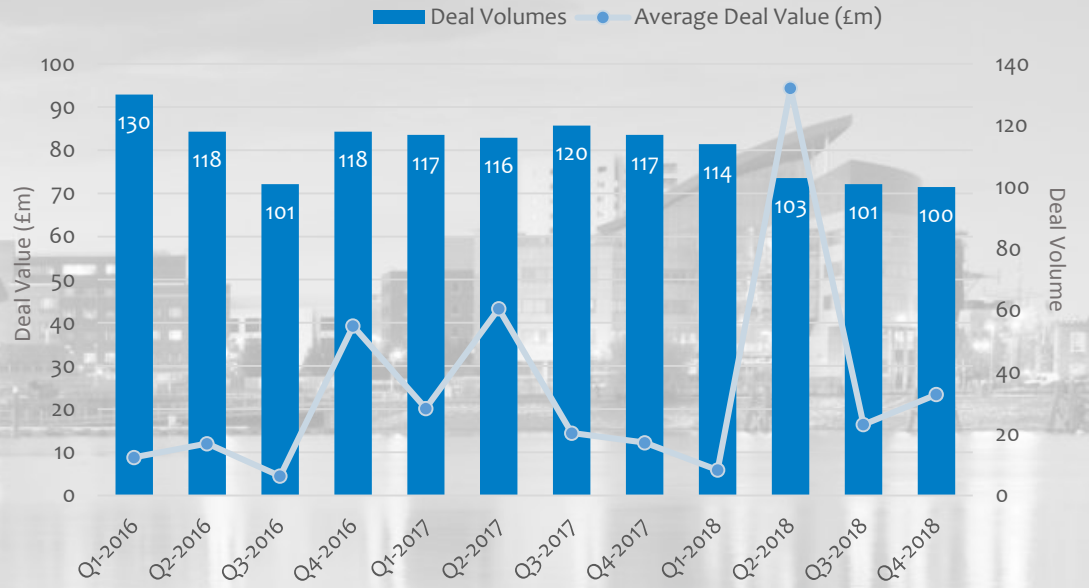
Human Capital M&A Activity Analysis

Overview

- Whilst deal volumes fell slightly in Q418, the market has shown resilience given continued political headwinds and challenges around Brexit uncertainty
- Deal volume decreased in the UK due to a decline in cross-border transactions originating in Europe, however strategic acquirers based in the United States and Asia continue to be active in the UK market
- Brexit remains a key impediment for activity in the European market with negotiations around the Irish border seeming the key determinant as to whether the UK leaves with an agreed deal or no deal
- Europe is still the most active market with domestic activity increasing in Q418, highlighting that, whilst political headwinds remain, there is a high level of confidence in the European market
- Demand for both temporary and permanent placements continue to increase, which coupled with falling candidate availability mean that a lack of supply is dragging on placement numbers. As a result those with high quality and available candidate pools are likely to attract increased interest from both strategic and financial acquirers
- Financial investors were increasingly active in Q418 and as succession is an industry wide concern for many business owners, it is expected that financial investors will become a larger driver of deal volumes as they look to back capable management teams and execute buy and build strategies
- Global stock markets had a disappointing Q418, a fall in share prices means that public interest companies are likely to be more acquisitive in the near term to boost earnings and address renewed shareholder pressure to reverse recent value erosion



Orion Managed Services Acquired by TechnoPro

- Japanese listed TechnoPro Holdings acquired a 60% stake in Orion Managed Services, a UK based specialist engineering recruiter
- The acquisition represents TechnoPro's first acquisition in the UK market and highlights that despite Brexit, the UK remains an attractive destination for investment
- Engineering recruitment is a sector that is experiencing high demand globally. This is driven by increased infrastructure spending and as a result it would be unsurprising to see more transactions of this nature as large strategic acquirers look to enter new geographies and access high quality candidate pools

Increased demand for temporary and permanent placements

- In the UK, candidate availability remains a concern for most industries, lack of supply means that permanent placements slowed in Q418
- Demand continues to grow for both temporary and permanent placements; offering growth opportunities to recruiters across both the private and public sector
- Within the permanent placement sector, accounting & finance and the engineering sectors saw the greatest increase in demand, driven by further growth in the underlying sectors
- Temporary recruiters benefited from increased demand over the Christmas period driven by the logistic and retail sectors
- It is expected that those with high quality and available candidate pools will attract interest from strategic and financial acquirers

Outlook for M&A Activity

- **Whilst global headwinds remain, key economies continue to enjoy strong recruitment fundamentals. This is driving domestic activity which is likely to continue in the near term**
- **As demand for both temporary and permanent staffing is increasing, acquirers will look to acquire those with high quality candidate pools to ensure continuity of service offering**
- **Following declining share prices and market ratings in December, public listed companies will look to make earnings enhancing acquisitions to boost market ratings**

M&A Market Review
Human Capital
Q4 2018

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Human Capital Global M&A Activity

North America

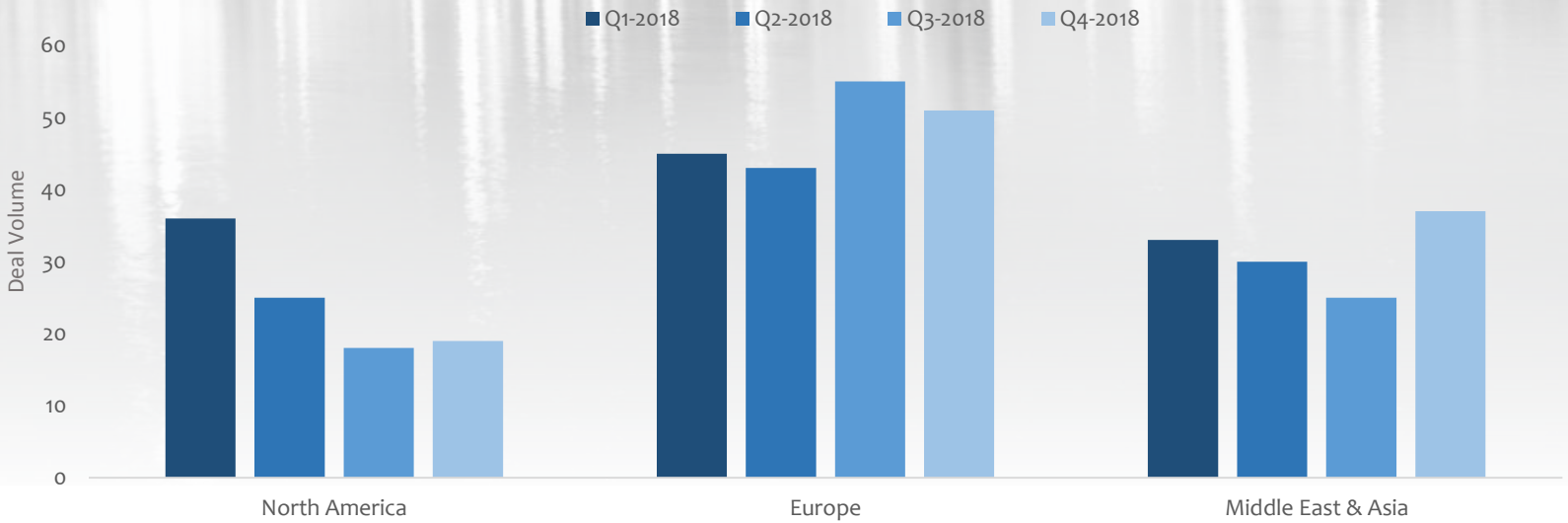
- M&A activity in North America increased in Q418, due to further investment by financial acquirers and consolidation in the healthcare and general staffing sectors
- US recruitment fundamentals have softened slightly with unemployment rising to 3.9% in December from 3.7% in November
- Transaction volumes are expected to increase due to continued positive recruitment fundamentals and drivers for consolidation in a number of sectors

Europe

- Activity within Europe fell slightly in Q418, mainly due to a decrease in cross-border transactions
- Brexit remains a key headwind for the market with activity expected to increase as clarity emerges
- The UK continues to be a major source of deal flow accounting for 43% of European M&A activity
- Strong recruitment fundamentals and pent up demand is likely to drive further activity in the near term

Middle East & Asia

- Transaction volumes rose significantly during Q418, driven by increased activity in Japan
- Japanese strategic acquirers within the online and general staffing sectors were the most active
- Financial acquirers invested heavily in the region over Q418, with a focus on the online sector
- Cross-border activity may have been subdued in the region, due to increasing political tensions



UK Inbound Activity

The UK remains one of the most active markets for Human Capital transactions. As the deadline for Brexit approaches, overseas acquirers have approached the market with a more cautious outlook. However, some overseas corporates such as Italian owned Gi Group have looked to expand service offering and market share. It is expected, that once Brexit uncertainty subsides, the UK market will see an upturn in activity and continue to attract attention from overseas markets

UK Outbound Activity

Outbound transaction activity decreased in Q418, with strategic acquirers looking to domestic markets for opportunities. It is clear that a number of larger corporates in the UK are adopting a "wait and see" approach on Brexit, which is suppressing activity levels. Once further clarity can be provided on the UK's future trading arrangements after Brexit UK strategic acquirers will pursue more ambitious international growth plans, driving outbound deal volumes higher

Outlook for M&A Activity

- **North American activity is expected to increase as a number of sectors continue to undergo consolidation, driven by strong recruitment fundamentals and falling candidate availability**
- **The European market remains highly active with increased levels of domestic activity. Cross-border transactions are likely to increase once clarity is achieved on future trading conditions in Europe**
- **Activity in the Middle East and Asia was once again driven by the Japanese market. The increased activity of financial acquirers in the region is particularly positive and suggests further activity is likely in the near term**

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Q4 2018

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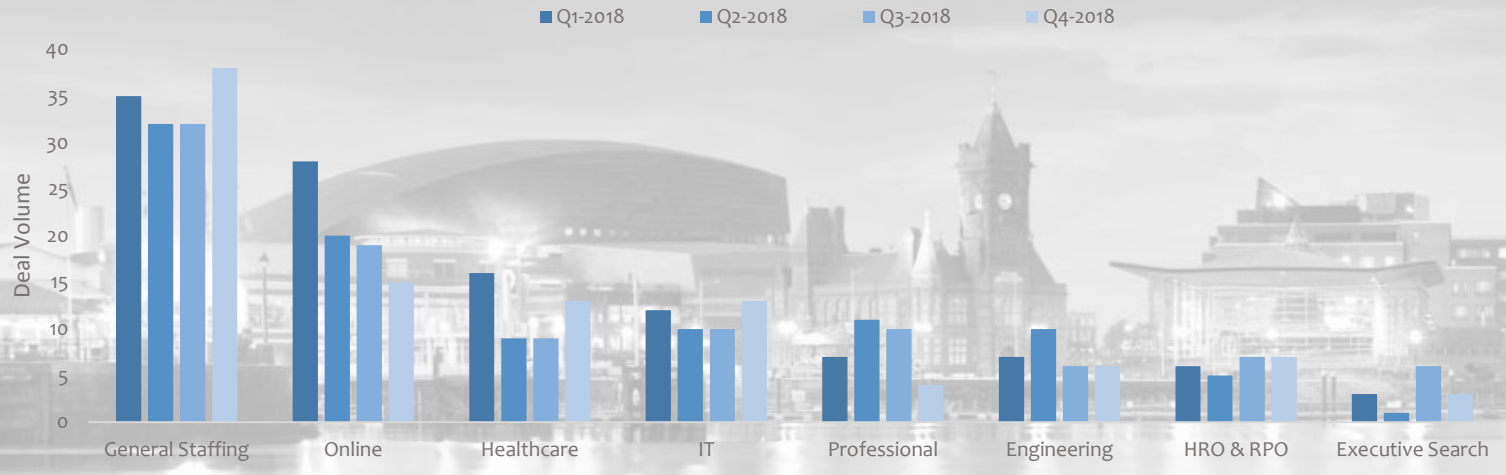
Human Capital Sub-sector Trends



19%

38%

General Staffing

Activity in the general staffing sub-sector increased significantly in Q418, and was again the most active sub-sector making up over a third of total transactions. The increased deal volumes were largely driven by a number of financial acquirers entering the market and strategic acquirers consolidating market share. Further consolidation is likely, due to decreasing candidate availability and increasing demand for staff across a number of key economies

5%

15%

Online

Overall transaction numbers fell in Q418, however, financial acquirers remain active within the sector. Candidate shortages are also driving strategic acquirers to look for organisations that connect with candidates in non-traditional ways. The outlook for the sector remains positive and competition between financial and strategic acquirers is likely to increase due to the increasing adoption of technology in the Human Capital market

0%

6%

Engineering

Deal volumes in the engineering sector remained at the same level as Q318, this is likely due to a shortage of sellers. Demand is increasing in the sector with infrastructure spending increasing globally which is likely to lead to increased consolidation in the sector as strategic acquirers look to ensure access to expertise. Within the UK, key industries such as the construction sector are expected to grow further, providing a positive outlook for the sector and could lead to increased deal volumes in the near term

30%

13%

Information Technology

Q418 saw the largest number of deals in the sector of any quarter in 2018. This was driven by falling candidate availability leading to further consolidation by strategic acquirers. Financial investors are also actively looking to the sector as they aim to back capable management teams and effect bolt-on acquisitions to existing portfolio companies. This is resulting in increasing competitive tension between strategic and financial acquirers which is likely to drive valuations and transaction volumes upwards

44%

13%

Healthcare

The healthcare recruitment sector underwent further consolidation in Q418 and transaction volumes increased by over 40%. Aging populations in a number of key economies are an increasing concern. Further consolidation is expected as incumbent providers are keen to take advantage of increasing billings and maintain candidate pool security. Key public sector organisation such as the NHS are increasingly reliant on temporary staff and as a result temporary specialists in the sector are attracting interest from both financial and strategic acquirers

= % growth Q3 2018 to Q4 2018

= % of transactions Q4 2018

M&A Market Review
Human Capital
Q4 2018

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Human Capital Public Comparables

Valuation Multiples

Public company EV/EBITDA multiples in the Gambit Human Capital Index fell in 2018 from 9.9x in Q118 to 7.7x in Q418, their lowest level since Q216. This reflects declining performance of global stock markets and economic headwinds, rather than being a comment on the strength of the Human Capital sector. Due to recent underperformance of the market, public interest companies are likely to come under renewed shareholder pressure to enhance market ratings and will look for value enhancing acquisitions

Company Name	EV/EBITDA			
	Q1 2018	Q2 2018	Q3 2018	Q4 2018
Adecco S.A. (SWX)	9.3x	8.5x	8.2x	7.5x
Brunel International NV (ENXTAM)	13.1x	22.4x	20.1x	17.3x
CPL Resources PLC (ISE)	8.7x	8.3x	8.0x	7.5x
Empresaria Group PLC (AIM)	4.6x	4.4x	4.7x	4.4x
Gattaca PLC (AIM)	5.9x	4.3x	4.4x	5.0x
Harvey Nash Group PLC (LSE)	6.2x	7.6x	8.0x	*
Hays PLC (LSE)	11.1x	11.0x	11.1x	7.5x
Impellam Group PLC (AIM)	6.9x	5.7x	6.4x	7.0x
ManpowerGroup Inc (NYSE)	8.5x	6.5x	6.4x	4.9x
Page Group PLC (LSE)	12.3x	12.1x	12.4x	9.7x
Prime People PLC (AIM)	3.5x	9.0x	6.6x	3.2x
Randstad Holding NV (ENXTAM)	10.6x	9.7x	9.1x	8.1x
Robert Half International Inc (NYSE)	11.5x	11.5x	13.0x	10.5x
Robert Walters PLC (LSE)	10.2x	12.5x	8.9x	7.1x
Staffline Group PLC (AIM)	5.9x	6.2x	8.7x	8.6x
SThree PLC (LSE)	8.6x	9.5x	10.0x	7.7x
Gambit Human Capital Index	**9.9x**	**9.2x**	**9.1x**	**7.7x**

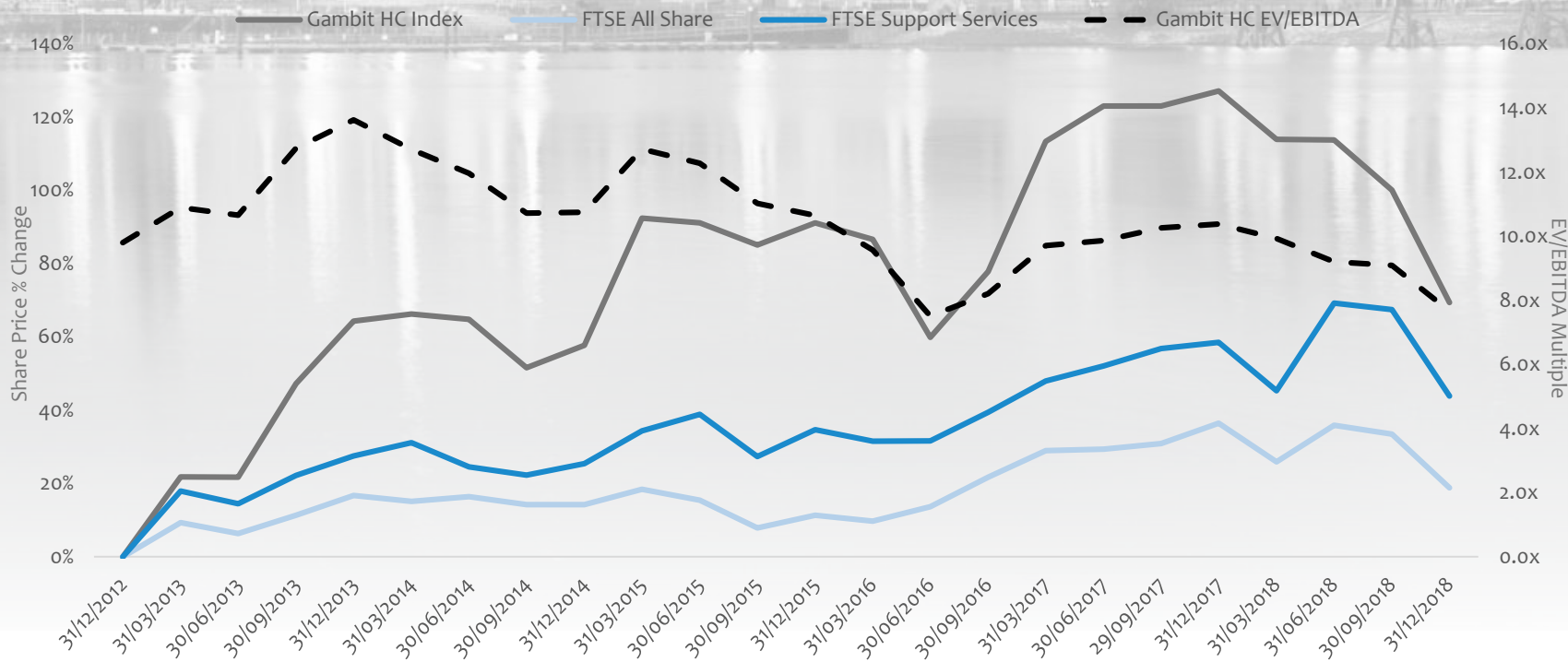
*Harvey Nash Group was delisted as a result of its acquisition by Dbay Limited which completed in Q418

Share Prices

Both the FTSE All-Share and the Human Capital Index tracked by Gambit Corporate Finance fell significantly in Q418. This was very much a global trend with most major indices finishing the quarter significantly down on their starting points. It is possible that the performance of the stock market in December was a market overreaction and share prices are expected to recover ground in the near term. Listed companies in the human capital sector are coming under pressure to ensure that market ratings improve in short-term and are likely to make earnings and value accretive acquisitions

Outlook for M&A Activity

- **Valuations and market ratings declined in Q418, however, this has put pressure on public interest companies to boost underlying earnings and market ratings. As the cost of capital remains low they are likely to be increasingly acquisitive and can pay higher multiples to exploit arbitrage opportunities**
- **The Human Capital sector remains cyclical in nature so, whilst the recent fall in valuations may suggest a market peak, market stability and asset availability will be key drivers of valuation in 2019**



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Key services include:

- Management Buy-outs/ Buy-ins
- Mergers and Acquisitions
- Fundraising/ Development Capital
- Financial Restructuring
- Private Equity Portfolio Advisory
- Succession Planning
- Refinancing
- Research and Deal Creation

CFI Group

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