gambit CORPORATE FINANCE 30 YEARS

Human Capital Market Review H2 2021

Introduction

This edition of Gambit's Human Capital market review highlights a degree of normalisation towards a sustainable level of M&A market activity and also sets out the key trends, considerations and areas of focus that business owners in the sector should be aware of. Despite temporary, Omicron-induced market volatility in Q421 the Human Capital sector exhibited signs of healthy consolidation activity, underpinned by confidence in the sector's resilience during times of short-term volatility. With acquirers placing ever greater emphasis on growing and driving resilience as a core value, we expect that the market will continue to remain buoyant.

With 2022 presenting new challenges, such as staff shortages and a race to diversify income streams, we expect financial and strategic acquirers will continue to deploy their pent-up cash reserves into the M&A market. Consolidators are leveraging what remains, for now, an accommodative borrowing environment. In 2022, the Human Capital sector is primed for its next wave of consolidation and Gambit continues to support Human Capital business owners with the execution of their strategic plans.

Geraint Rowe
Partner, Human Capital

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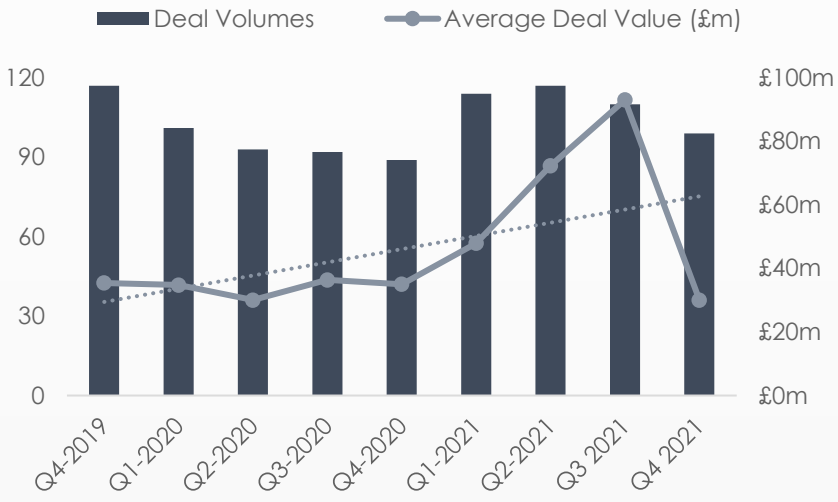
Director, Human Capital

H221 Summary

- **H221 exhibited signs of normalisation towards sustainable levels of activity, driven by well capitalised acquirers remaining active and eager to deploy pent up cash reserves.**
- **Despite Omicron-induced fears, UK companies have attracted sustained levels of appetite as the third most active Human Capital M&A market in H221, behind only the US and Japan, driven by high quality UK assets and appetite from domestic and financial acquirers.**
- **UK deal values increased by 23% between H121 and H221 fueled by significant domestic recruitment activity and a growing awareness of the important role that Human Capital companies are playing in facilitating post-pandemic strategies through talent led solutions.**
- **H221 saw a rise in General Staffing, HRO & RPO, Engineering and Executive Search sub-sector transactions, on the back of skills shortages, increased administrative burdens, committed private and public sector investment in infrastructure and a growing impetus to reset company strategies and strengthen management teams.**
- **With 65% of hirers struggling to source suitable candidates (REC), companies are willing to pay premium placement fees for specialist recruitment services, positively enhancing profitability in 2022 during a period where market valuations still exceed pre-pandemic levels.**
- **In 2022, we expect to see a marked increase in debt funded Human Capital M&A activity, with acquirers sourcing external finance to fund growth strategies leveraging what, in the short term, will remain an accommodative and low interest rate borrowing environment.**
- **With Human Capital companies accumulating significant cash balances and private equity firms accruing record levels of 'dry powder', both will seek to deploy resources into quality assets and in-demand, profitable sub-sectors, which will drive buoyant Human Capital M&A activity in 2022.**
- **With Omicron concerns averted in the UK and multiples rebounding in the early stages of 2022, there is an opportunistic 'window of opportunity' for shareholders to explore succession strategies while transaction activity and competitive tension can be leveraged to maximise value realisation.**

"Confidence in the sector's resilience during times of short-term volatility is driving buoyant levels of M&A and we expect a wave of consolidation activity in 2022."

Global M&A: Activity



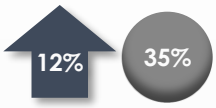
Company Name	EV/EBITDA			
	Q1 2021	Q2 2021	Q3 2021	Q4 2021
Adecco S.A. (SWX)	12.0x	11.0x	7.7x	7.4x
Brunel International NV (ENXTAM)	9.2x	9.1x	7.5x	8.5x
Empresaria Group PLC (AIM)	2.8x	4.8x	5.2x	5.0x
Gattaca PLC (AIM)	12.1x	30.3x	33.5x	5.3x
Hays PLC (LSE)	27.3x	29.2x	29.8x	13.7x
Impellam Group PLC (AIM)	2.9x	3.5x	5.8x	7.0x
ManpowerGroup Inc (NYSE)	11.2x	13.2x	9.0x	7.4x
Page Group PLC (LSE)	11.6x	22.4x	14.2x	14.5x
Prime People PLC (AIM)	5.7x	6.5x	14.4x	4.9x
Randstad Holding NV (ENXTAM)	11.3x	11.7x	9.1x	8.5x
Robert Half International Inc (NYSE)	20.1x	25.5x	19.7x	17.1x
Robert Walters PLC (LSE)	7.6x	11.8x	8.8x	9.2x
Staffline Group PLC (AIM)	7.3x	11.8x	5.6x	5.2x
SThree PLC (LSE)	10.5x	12.6x	12.4x	9.9x
Gambit Human Capital Index	**12.4x**	**13.7x**	**10.3x**	**9.5x**

Overview

- With significant pent up demand driving deal volumes beyond pre-pandemic levels in H121, our analysis for H221 shows signs of normalisation towards a sustainable level of activity with well capitalised acquirers remaining active and driving what is overall a very buoyant market.
- Despite the correction in Q421, caused by heightened global concerns around the Covid-19 Omicron variant at the end of the 2021, H221 Human Capital sector transaction values rose by 2.3% on H121 and were 84% higher than H120.
- In contrast, UK deal values increased by 23% between H121 and H221 fueled by significant domestic recruitment activity, which has seen record levels of vacancies and a growing awareness of the important role that Human Capital companies are playing in facilitating post-pandemic strategies through talent led solutions.
- The UK was also the third most active Human Capital M&A market in H221, behind only the USA and Japan, driven by high quality UK assets and appetite from domestic and financial acquirers
- Strong UK M&A activity is likely to be sustained in view of trends such as domestic staff shortages, the significant cash reserves of publicly listed Human Capital companies and the potential for inflationary pressures to significantly affect the associated cost of capital to fund M&A activity.
- Omicron fears and tighter central bank policies tempered EV/EBITDA valuations in the Gambit Human Capital Index in H221, with a general fall in market capitalisations of large listed recruiters such as Adecco and ManpowerGroup causing the average multiple of our index in H221 to reduce by 24% when compared with the H121 average.
- There was an element of polarity in the fortunes of companies in our index, illustrated by Gattaca's significantly lower profits due to the delayed recovery of its contract business, the news of which cut its share price in half in December 2021, from a three year high in June 2021.
- **With Omicron concerns averted in the UK and multiples rebounding in the early stages of 2022, there is an opportunistic 'window of opportunity' for shareholders to explore succession strategies while transaction activity and competitive tension can be leveraged to maximise value realisation.**

Sub-Sectors in Focus

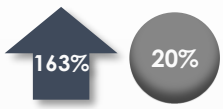
General Staffing



- General Staffing sub-sector M&A activity has remained strong, with deal volumes increasing by 12% from H121 to H221, supported by significant demand from hirers looking to fill an unprecedented level of vacancies.
- With skills shortages rife throughout the UK economy, companies are leveraging the diverse knowledge of General Staffing firms to procure quality employees, with businesses acknowledging that expert recruiters are vital to achieving long-term growth plans.
- Inflation is set to have a significant and persistent effect on international labour markets and coupled with widespread cost of living challenges, we expect that this will result in sustained demand for General Staffing services, which will contribute to buoyant deal volumes and values in 2022.

65% **Hirers struggling to source suitable candidates**
Source: REC, 2021

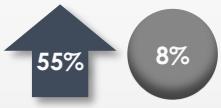
HRO & RPO



- HRO & RPO has emerged as the fastest growing Human Capital sub-sector for M&A activity, with deal volumes increasing by 163% from H121 to H221.
- Significant demand for HRO & RPO providers has been underpinned by the expertise and assistance of quality assets in key markets such as the UK, who are relieving companies of administrative burdens and easing the complexities of tightened regulatory compliance caused by Brexit and IR35, allowing companies to focus on strategic plans.
- With 60% of European companies currently considering outsourcing as a method of streamlining their business operations, we expect that the HRO & RPO deal volumes seen in H221 signals the start of a period of heightened consolidation in the sub-sector, contributing a higher proportion of overall Human Capital M&A activity going forward.

60% **European companies outsourcing, or considering outsourcing, their payroll management**
Source: SD Worx, November 2021

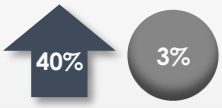
Engineering



- The Engineering sub-sector has re-emerged as one of the most active areas of Human Capital M&A activity, with deal volumes rising by 55% from H121 to H221, underpinned by a STEM skills shortage and accelerating technological advancements.
- The UK is experiencing an acute STEM skills shortage, with 50% of engineering firms struggling to recruit candidates with appropriate knowledge and skills (The Manufacturer), driving hirers towards specialist Engineering recruitment firms, who have the access and ability to source quality talent.
- With multi-line recruiters increasingly looking to gain exposure to the Engineering sub-sector and large levels of committed private and public sector investment in infrastructure, we are optimistic that this will lead to buoyant levels of M&A activity in 2022.

83% **Engineering staffing firms reporting positive year-over-year revenue growth**
Source: SIA, November 2021

Executive Search



- The Executive Search sub-sector saw deal volumes increase by 40% from H121 to H221.
- The stark rise in M&A activity 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.
- 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.

£1.7bn **Forecast value of the Executive Search industry by 2027**
Source: IBISWorld, November 2021

% change in deal volume from H121 to H221

% total deal volume in H221

2022 Trends and Outlook

With significant levels of market activity expected in 2022, we set out below the most commonly cited trends that businesses in the sector are faced with and outline how the outlook for M&A activity will be affected in 2022.

Skill Shortages

- There has been a marked improvement in business confidence which has reignited companies' expansion plans, driving a resurgence in recruitment activity which, in turn, has amplified the UK's acute skills shortage, with 65% of hirers struggling to source suitable candidates (REC).
- As a result of the UK's skills shortage, hirers are increasingly reliant on the expertise of the UK Human Capital sector, leveraging specialist recruitment firms to improve their access to quality candidates, as part of long-term talent acquisition strategies.
- **Whilst presenting challenges, this trend also presents the sector with a significant opportunity as hirers are willing to pay premium placement fees for specialist recruitment services, positively enhancing profitability during a period where market valuations continue to exceed pre-pandemic levels.**

Significant Cash Reserves

- Cash reserves of publicly listed Human Capital companies have more than doubled over the last twelve months, presenting significant resources to undertake greater levels of strategic M&A and corporate development activity which will drive buoyant deal volumes and EV/EBITDA multiples in the Human Capital market.
- The private equity market accrued an estimated £1.3tn of 'dry powder' pre-pandemic, and the initial deployment of these funds elevated private equity M&A activity in 2021 to its highest annual level on record.
- **With Human Capital companies accumulating significant cash balances and private equity firms accruing record levels of 'dry powder', both will seek to deploy resources into a fragmented market with quality assets and in-demand, profitable sub-sectors, which will drive buoyant Human Capital M&A activity in 2022.**

84% ***Rise in Human Capital deal values from H120 to H221***
(Gambit Analysis, January 2022)

15,640 ***Temporary employment placement agencies in the UK***
(IBISWorld, June 2021)

£29.4bn ***Total amount of money flowing into UK Technology industry in 2021***
(UK Government, December 2021)

$6tr ***Total value of the private equity market***
(Preqin, November 2021)

Technology

- A sense of urgency has been created to acquire quality 'bolt-on' assets to augment existing offerings and broaden technological capabilities, in order to ensure that recruiters continue to move up the value chain and avoid a stagnation in their service offering.
- As staffing firms increasingly invest in automation, the rise in the prominence and importance of the recruitment platform ecosystem has intensified in recent years, with significant levels of M&A, investment and partnerships expected in 2022.
- **With a convergence in the portfolios of staffing firms, talent platforms and online services, increased competitive tension will drive deal values upwards, offering sellers a 'window of opportunity' to capitalise.**

Inflationary Pressures

- The Bank of England raised interest rates from 0.1% to 0.25% in December 2021, for the first time in more than three years. This announcement is expected to be the first in a series of interest rate rises over the short and medium term, casting doubt over the longevity of the current low cost of capital environment.
- With interest rate rises firmly on the domestic agenda, there is a heightened sense of urgency to execute debt funded transactions before borrowing becomes more expensive.
- **In 2022, we expect to see a marked increase in debt funded Human Capital M&A activity, with acquirors sourcing external finance to fund growth strategies, leveraging what, in the short term, will remain an accommodative and low interest rate borrowing environment.**

Gambit Corporate Finance

Key Points in Focus

- The current M&A environment presents a 'window of opportunity' for shareholders to explore succession strategies while transaction activity and heightened competitive tension can be leveraged to maximise value realisation.
- The UK market is currently highly fragmented, offering Human Capital companies the unique opportunity to create significant value through bolt on acquisitions that facilitate greater portfolio diversification or increased market share.
- The outlook for the Human Capital sector in 2022 is strong, as hirers leverage recruiters to combat skill shortages, strategic and financial acquirers deploy pent up cash reserves and dry powder, and the currently favourable borrowing environment contributes to an enhanced level of M&A activity in the medium term.
- Proactive business owners should reach out to their advisory network to establish a best practice approach to maximise value creation and realisation opportunities.

Gambit's Added Value Approach

- Gambit's Human Capital expertise and dedicated research function enables us to identify off-market acquisition targets and assess acquirer appetite, whilst our close-knit relationships with the private equity market affords our client base targeted exposure to financial investors.
- Gambit's detailed knowledge and insight into the Human Capital market enables us to advise on appropriate valuation metrics and present opportunities to appropriate acquirers, targets and/or funders.
- We maintain regular dialogue with our international colleagues within Corporate Finance International (CFI), sharing cross-border opportunities, sector trends and transaction insights, underpinning constructive negotiation of transactions resulting in a commercial and optimal outcome.
- Gambit acts as an extension to senior management teams, with a service that is genuinely partner-led by like-minded business owners, available 24/7 to discuss commercial issues or provide a sounding board, priding ourselves on the strong, long-lasting and collaborative relationships we build with our clients.
- In an increasingly active M&A market, Human Capital business owners should look to utilise experienced corporate finance advisors to support strategic decision making and maximise value realisation, leveraging the currently buoyant level of M&A market activity.

Benefits of Gambit

- A team of highly experienced specialists
- Focussed on value creation and maximisation
- Commercial focus and attainment of shareholder objectives
- Significant cross-border capability as exclusive UK shareholder of CFI
- Deal risk minimisation
- 24/7 availability

Key Services Include

- Mergers & acquisitions
- Disposals
- Management buy-outs
- Fundraising
- Development capital
- Debt advisory
- Private Equity advisory
- Refinancing
- Value Maximisation Reviews
- Succession planning
- Strategic advice

Gambit Corporate Finance

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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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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 23 offices throughout the world, CFI members specialise in cross-border acquisitions, disposals, capital raising, and related services. CFI have advised on a significant number of staffing sector deals and is ranked number 19 in Europe and 26 globally by Thomson Reuters for transactions valued up to €200 million.

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