

RECRUITMENT
SECTOR INSIGHTS

2018 | BDO MERGERS & ACQUISITIONS





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INTRODUCTION



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The UK recruitment sector continues to be attractive to investors despite the evident challenges on the horizon.

The past year has shown a continuation of the high levels of demand for talent in the UK, supported by the country's four-decade low unemployment rate of 4.3%. This high level of employment comes at a time where, in Brexit, the economy faces its biggest challenge since the financial crisis. The market as a whole continues to show resilience to this potential threat with a record number of new recruitment agencies formed in the UK during 2017 at over 9,000.

This positive sentiment in the market is reflected in M&A activity throughout 2017 with 116 transactions completed globally, continuing the high volume of recruitment deals we've seen over the last few years.

Similar buoyancy has been seen in the wider UK market where management buy-outs rose to the third highest levels ever recorded in 2017 at £27.8bn, a doubling of the levels seen in 2016.

Whether due to the continued investor confidence in the UK market's resilience or the weakening of the Pound, external investment into the country has continued with over 20% of transactions this year involving an overseas buyer.

Private equity fondness of the sector also shows no signs of waning. The number of deals from institutional investors is up 35% on last year.

The challenges to the market from Brexit and political uncertainty are obvious. Following years of sustained growth the market is forecast to flat-line over the next 3 years in an environment where staffing decisions are potentially pushed back until the political landscape smooths out.

We also need to be mindful of the impact of large corporate failures on the wider UK economy in terms of investor and buyer confidence. In the wake of the recent collapse of Carillion, the adjacent supply chain faces significant challenges in the coming months and might soften investment appetite into related sectors in the short term.

We take a look at Brexit and other trends impacting the recruitment sector in this report. We will also highlight key trends in the M&A market during 2017 and an outlook going forward into 2018.

UK RANKED NO.2 GLOBALLY

for M&A transactions in the recruitment industry consistently since 2012.

EDUCATION AND IT

sectors accounted for 14% of UK M&A transactions each in 2017.

3% DECREASE

in the number of M&A deals in 2017 from 2016 with a total of 116 completed.

SUSTAINED INVESTMENT INTO THE UK

with 23% of UK transactions involving an overseas buyer.

PRIVATE EQUITY ("PE")

involvement in deals increased 35%. PE also accounted for almost 40% of total transactions globally in 2017.

UK RECRUITMENT MARKET

THE INDUSTRY IN 2017

THE MARKET

The UK recruitment market has continued to grow throughout 2017 with a total revenue of £12.8bn. This represents an impressive growth rate of 3.4%.

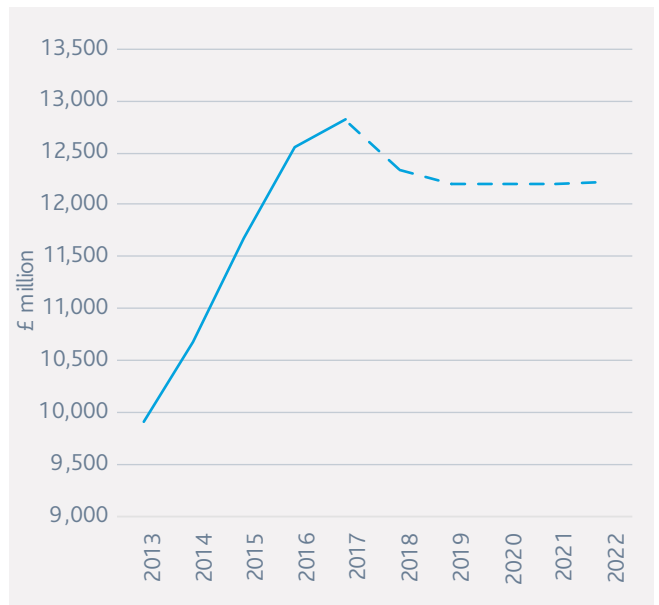
Growth in the recruitment sector closely follows that of the UK economy. We are currently in a period where businesses are showing robust confidence levels and continuing to invest in people. This is echoed by the 40 year high employment rates in the country.

In light of the uncertainty over Brexit, falling consumer spending and the subsequent predicted impact on business confidence, it is forecast that the UK recruitment market will enter a period of retraction through to the end of 2019.

The market is expected to recover in 2020 as the economy adapts to the new conditions after leaving the EU. During the intervening period we expect there to be both winners and losers within the industry. Firms who operate in areas characterised by skills shortages and those in part which are insulated from macro-economic pressures will continue to thrive.

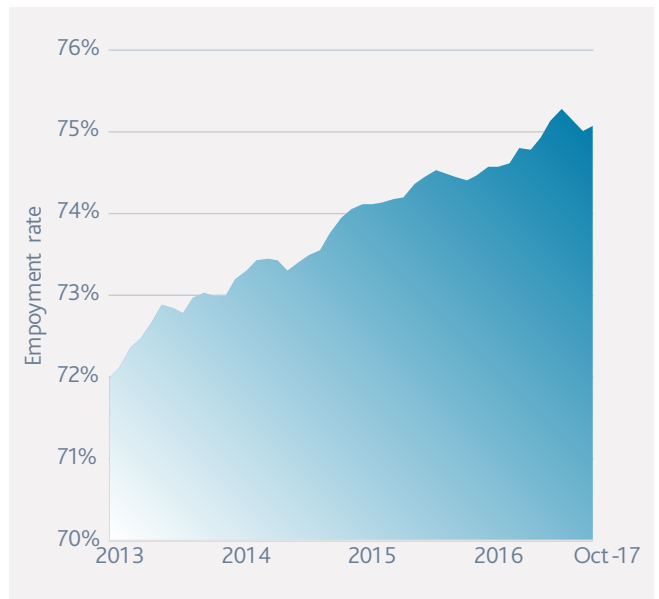


Figure A: UK Recruitment Market



Dashed line represents forecast figures
Source: IBISWorld

Figure B: UK Employment Rate



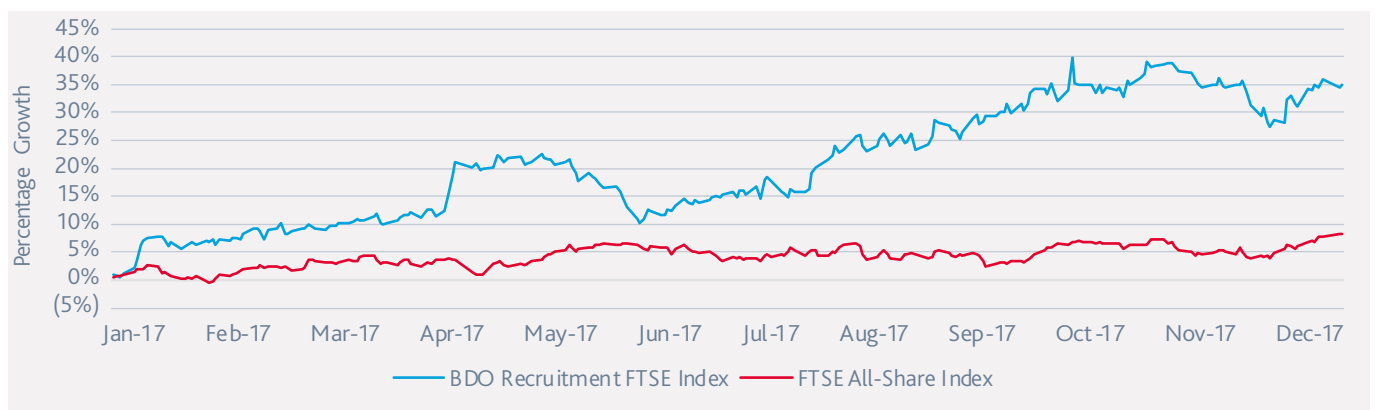
Source: Office for National Statistics

UK RECRUITMENT MARKET

CAPITAL MARKETS

Continued strong performance from the UK listed recruitment businesses as they once again outperform the general market.

Figure C: BDO FTSE Listed Recruitment Firms vs. FTSE All-Share Index in 2017



Source: Capital IQ

Capital markets are able to provide a view on the general investment sentiment around the recruitment industry. The BDO FTSE Recruitment Index comprises listed recruitment firms here in the UK that represent the overall market. This has been compared to the FTSE All-Share Index by aggregating the recruitment share prices and rebasing to the start of 2017.

The BDO FTSE Recruitment Index has performed strongly and continued to outperform the wider market in terms of capital growth, which is consistent with the past four years. At the end of 2017, the BDO FTSE Recruitment Index had grown by 35% from the beginning of the year, clearly impacted by improving economic growth and falling unemployment rates in the UK.

Peaks and troughs have been present in both the share price growth and multiples, highlighting the volatility of the recruitment sector to macro-economic factors. One such example is the share price spike in April in reaction to news of a snap general election despite the overall market falling.

The average EV/EBITDA multiple shows a steadily increasing trend from an average of 9.1x at the start of the year to 10.8x at the end of December. This represents an impressive 17% increase through the year.

The peak in September primarily stemmed from an 8% jump in Hays plc share price following the announcement of annual results with operating profit up 21%.

Figure D: BDO FTSE Listed Recruitment Firms Average EV/EBITDA Multiple



Source: Capital IQ

UK RECRUITMENT MARKET

KEY TRENDS

BREXIT

As talks progress over what the UK leaving the EU will look like, a picture is beginning to form of the country post-Brexit. There does however, remain uncertainty over what future trading with our European neighbours will look like and how it might affect immigration laws.

This uncertainty is likely to manifest itself through a decline in business confidence which could further compound the problem with organisations freezing recruitment plans until the landscape becomes clearer. Candidates may also be less likely to consider career moves while they are unsure of the outlook, reducing firms' ability to fill vacancies.

There may be an opportunity in some sectors as overseas workers decide to leave the UK, creating a skills gap that recruiters can fill.

Source: CIPD

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TRANSACTIONS IN SOFTWARE AND ONLINE PLATFORMS IN THE LAST TWO YEARS

UK SKILLS SHORTAGE

By the middle of next decade, 21.8m people will be chasing low and intermediate-skilled jobs with a surplus of candidates of 8.1m. In contrast, there will be 4.2m highly skilled jobs that cannot be filled by the right candidate, according to the Learning and Work Institute. This issue is affecting the service sector most severely.

The impact of this skills shortage on the recruitment industry will necessitate a targeted approach to fulfilling roles with the right candidate through research, lengthier selection processes and potentially the provision of training as part of the recruitment process.

Source: Confederation of British Industry

72%

OF FIRMS EXPECT AN INCREASE IN COMPETITION FOR TALENT DUE TO BREXIT

TECHNOLOGY

Availability of information through the internet and social media has made the connection between candidate and recruiter much more straightforward. This does also pose a potential threat as there is now a direct line between candidate and potential employer. Candidates are able to apply for jobs directly to employers through new online platforms. Recently McDonald's ran a recruitment campaign through the app Snapchat.

The challenge for recruiters is to deliver the service and value-add to businesses in finding the right candidate for the right role.

The importance of this in the market place has been reflected through increased investment in technology and consolidation in the market place as the big firms target, through M&A, those with the software to drive their recruitment offering forward.

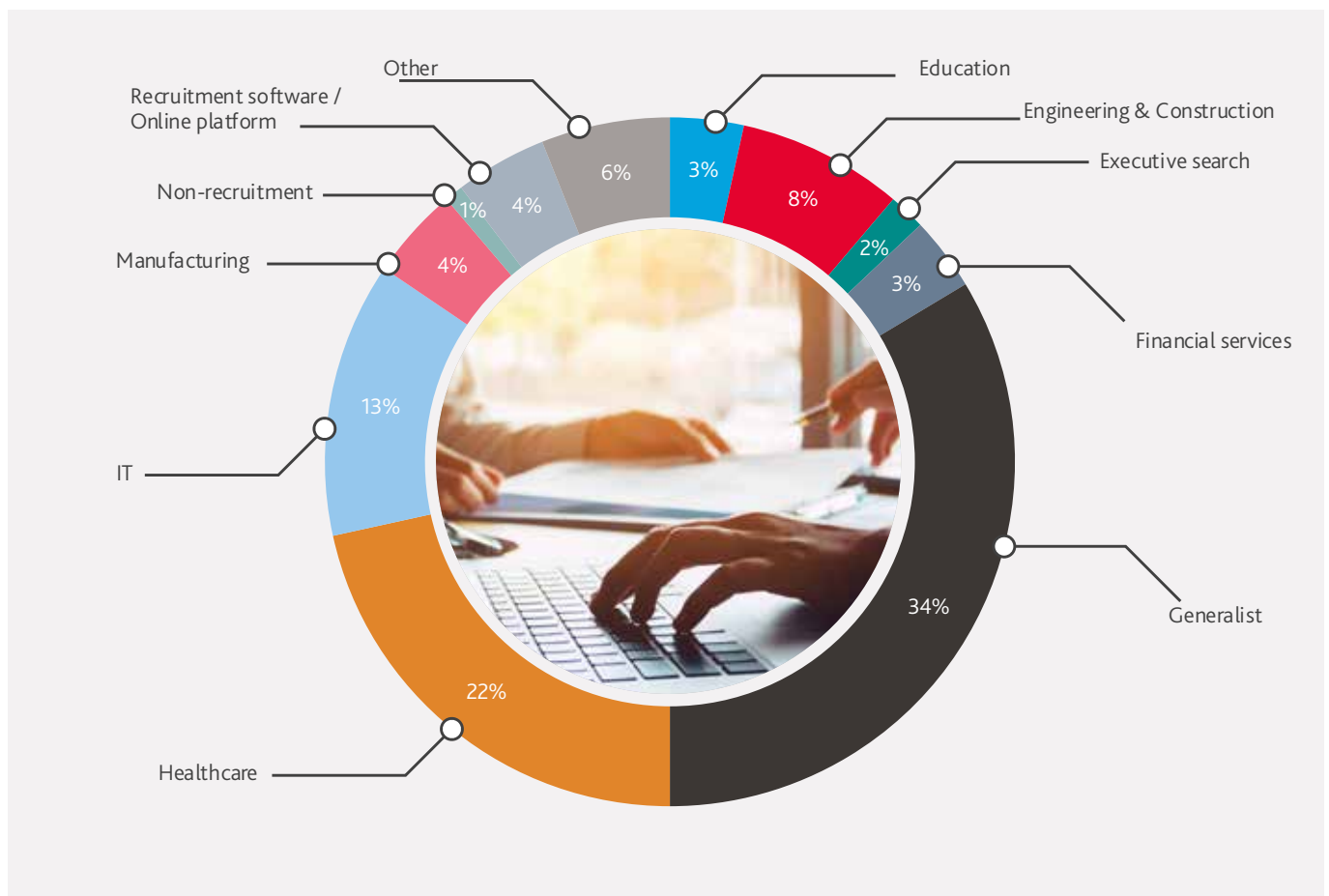
Source: MergerMarket

SERVICE SECTOR SKILLS SHORTAGE AT ITS WORST LEVEL FOR 19 YEARS

M&A ACTIVITY

GLOBAL DEAL REVIEW 2017

Figure E: 2017 Worldwide Recruitment Deals by Vendor Sector



Source: MergerMarket

* Other relates to sectors with only one transaction in the year

Private equity investment in recruitment has increased again year on year. Fund managers are attracted to firms operating in niche, growing sectors with strong management teams.

The trend of investment in technology continues with online platforms and recruitment software making up an increasing proportion of deal activity.

Healthcare continues to be the most appealing specialist sector for investment, accounting for 25 transactions this year. 80% of these occurred in the US.

The number of deals in the IT sector continues to grow as activity moves away from traditional sectors including industrials and manufacturing.

The focus for M&A has been towards those recruitment firms with sector specialisms, particularly within private equity-backed deals.

M&A ACTIVITY

INVESTMENT PATTERNS

TRANSACTIONS BY COUNTRY

The US and UK continue to be the most active regions in the recruitment market for mergers and acquisitions with 48 and 22 transactions respectively in 2017.

The US has been driven by the healthcare sector with 42% of total 2017 transactions being in this area. The causes are twofold; consolidation for larger players in the market as they target smaller competition and institutional investors being attracted to the market for strong returns.

Deal activity in the UK is split more broadly across the industry with only two sectors accounting for over 10% of transactions, Education and IT.

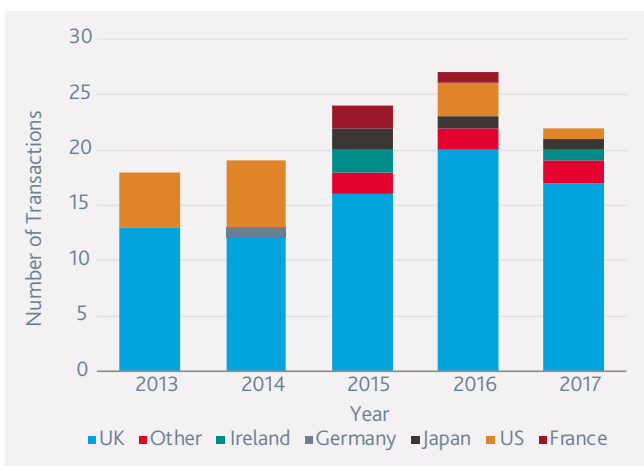
This reflects the high level of employment over the UK and mirrors the skills shortage in the education and technology sectors where both the government and private businesses are seeking to invest further.

PRIVATE EQUITY

Private equity involvement in UK transactions has doubled on the previous year. The firms being targeted are largely specialists as the PE houses are able to understand the sector and in some cases implement 'buy & build' strategies.

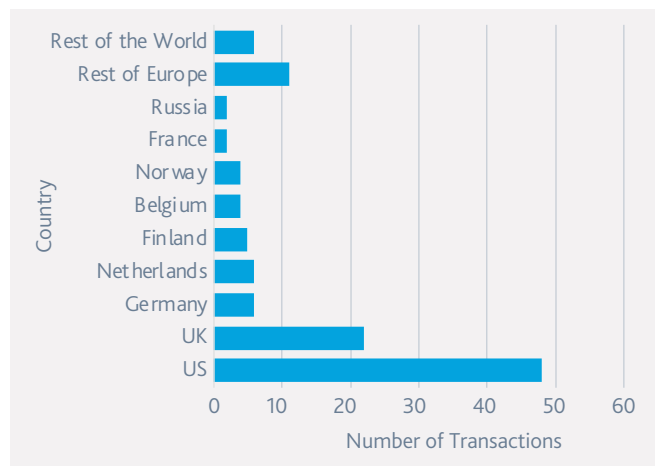
An example of this is the education sector where we have seen Graphite Capital acquire two assets in 2017 (Empowering Learning and Timeplan Education), building on Sovereign Capital's foray into the sector in 2015/2016 with the purchase of Synarbor plc and subsequent bolt on acquisition of Just Teachers in 2016.

Figure F: Investment into the UK by Country



Source: MergerMarket

Figure G: Global Deals by Country



Source: MergerMarket

TECHNOLOGY

The trend of investing in technology has continued as firms seek to get ahead with software. This has resulted in large firms in the recruitment software sector merging or acquiring smaller businesses to consolidate their position and offering.

One example in 2017 of this is the Bond International and Erecruit merger which brings together two of the US' largest staffing software providers.

UK MARKET

The total number of transactions in the UK has dropped to 22 from a five year high in 2016 of 27. Therefore, demand remains strong for UK recruitment assets however the fall in activity below 2015 levels is indicative of the uncertainty and lower business confidence forecast into 2018/19 from Brexit. Despite manufacturing output being at a 10 year high (source: CIPS), this sector along with construction saw a drop off in recruitment M&A deal volumes in 2017 as businesses take stock.

Interest from outside the UK remained strong through 2017 with 23% of the investment for UK businesses coming from overseas in 2017. This highlights that market sentiment, overall, is positive with low unemployment and skill shortages in specific UK sectors. In part, this is also due to the depreciated Pound which has made UK assets attractive to global investors seeking undervalued opportunities.

The lack of skilled staff provides an opportunity for recruitment firms in developing a specialisation – which is particularly attractive to investors. One such example being the Inflexion investment into K2 Partnering Solutions who specialise in recruiting IT experts in Big Data, AI and robotics.

DEAL HIGHLIGHTS

A SELECTION OF 2017 TRANSACTIONS

MERGER IN RECRUITMENT SOFTWARE

BOND INTERNATIONAL AND ERECRUIT MERGE

In June 2017 Bond International and Erecruit merged to bring together two of the leading staffing software developers in the US. The goal is to offer the most comprehensive global staffing software platform available.

CONSOLIDATION IN THE HEALTHCARE SECTOR

CROSS COUNTRY HEALTHCARE ACQUIRE ASSETS OF ADVANTAGE RN

As part of a trend of consolidation in the US healthcare sector, Cross Country acquired the assets of Advantage in June 2017 for a reported \$88m. The strategic rationale being to increase their foothold in the market place.

PLC RECRUITMENT FIRM INVEST IN IT SECTOR

HARVEY NASH PURCHASES CRIMSON LIMITED FOR £12M

Harvey Nash have invested further in their IT recruitment offering through the purchase of Crimson Limited for £12m in September 2017.

US INVESTMENT INTO UK RECRUITMENT MARKET

STAFFING 360 SOLUTIONS ACQUIRE UK BASED CBS BUTLER FOR £14M

As part of their international growth strategy, Staffing 360 paid £14m for CBS Butler, the engineering and IT recruitment specialist.

Staffing 360 also acquired firstPRO for a consideration of \$8m. Both the acquisitions, will add revenues of \$256m to Staffing 360's forecasted earnings.

PE HOUSE BACKS PUBLIC SECTOR RECRUITER

ENDLESS LLP ACQUIRES CER STAFFING SOLUTIONS LIMITED (AFFINITY WORKFORCE) FOR £25M

Endless bought into the healthcare and education recruitment market in June 2017 through the purchase of CER, from Capita, who focus on public sector placements.

PE INVESTS INTO SPECIALIST IT RECRUITER

K2 PARTNERING SOLUTIONS FUND RAISE WITH INFLEXION

Inflexion Private Equity Partners have acquired a minority stake in K2 for an undisclosed consideration. The specialist firm recruits for businesses in IT for AI, robotics, Big Data and social media.

SALE OF US LISTED AGENCY RECRUITMENT BUSINESS

HUDSON GLOBAL SELLS OFF INTERNATIONAL OPERATIONS

In three separate transactions, Hudson Global sold the recruitment arms of its business to focus on recruitment process outsourcing.

The firm's Benelux recruitment and talent management operations were sold to Dutch firm Value Plus for \$24.7m. The rest of Europe was acquired by Luxembourg-headquartered Morgan Philips for \$10.5m. Asia Pacific operations were sold to Australia-based Apache Group as part of an MBO led by Hudson Asia Pacific CEO Mark Steyn for \$6m.

JAPANESE PLC GROWS UK PRESENCE

TRUST TECH INC. ACQUIRED GAP PERSONNEL FOR £17M

Trust Tech, listed on the Tokyo Stock Exchange, paid £17m for the Welsh-based firm Gap Personnel who specialise in manufacturing placements in order to develop the UK market.

BDO MERGERS & ACQUISITIONS

BDO UK

8 Offices **260** Partners
1 **3,600** Staff

FOR THE **THIRD YEAR RUNNING**
MORE OF OUR CLIENTS **95%**
WOULD RECOMMEND US
THAN **ANY OTHER FIRM¹**

2016/2017 RESULTS:
REVENUES² UP **4.8%** TO **£456m**

¹ Independent research (I&D Market Monitor 2013-2017) by MeridianWest shows that BDO, for the third year running, have the highest proportion of clients who would recommend their advisers among its peer group

² Cross Revenue

BDO CORPORATE FINANCE UK

300 COMPLETED DEALS IN 2017
WITH A TOTAL DEAL VALUE OF **£18.5bn**

40% PRIVATE EQUITY DEAL INVOLVEMENT **25%** OF OUR DEALS ARE CROSS BORDER

ONE OF UK'S MOST ACTIVE ADVISERS*

AN **AWARD WINNING** CORPORATE FINANCE BUSINESS

200 CORPORATE FINANCE PROFESSIONALS IN THE UK

*3rd most active financial adviser in the UK - Experian league tables 2017
*4th leading DD provider in the UK - Mergermarket league tables 2017

BDO INTERNATIONAL

US\$8.1 billion 2016/2017 REVENUE
A YEAR ON YEAR INCREASE OF **8%**

162 Countries **1,500** Offices
74,000 Staff



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