Human Capital Management

MARKET UPDATE | JULY 2020

Human Capital Management Market Update: July 2020

With the gradual reopening of the U.S. economy and many firms reporting a “leveling off” in their business after steep April declines, human capital management (HCM) firms are beginning to shift their strategic focus toward growth-oriented investments and strategies to capitalize on a return to market growth.

Summary HCM Perspectives and Observations

The overall impact of the COVID-19 pandemic to the HCM sector has been mixed, depending on end-market exposure. Many businesses hit particularly hard have been forced to reduce their workforce, institute mandatory hiring freezes, and execute significant variable cost reductions. These actions have disproportionately impacted contingent workers; within the U.S., for example, temporary employment occupations declined 29.2% in April as opposed to a 13.5% decline in overall employment.[1] Despite the difficult environment, there are reasons for both near-term and long-term optimism regarding the HCM industry as a whole:

1. An increasing number of executives have indicated a late April market “bottom,” with weekly revenue declines replaced by relatively stable, and in some cases growing, headcount throughout May and June.
2. While still heavily focused on liquidity and liability management, conversations with HCM executives and investors are increasingly including more serious discussions around M&A opportunities from both a buyside and sellside perspective.
3. Firms with a presence in markets impacted early by the COVID-19 pandemic (e.g., China and Japan) continue to indicate a slow but accelerating return to “normal,” a hopeful sign for the trajectory of recovery in Europe and North America.
4. Public markets appear to have internalized the downward pressure on earnings for 2020; HCM share prices have trended upward from April lows, and forward multiples are hovering at, or above, pre-COVID-19 averages.

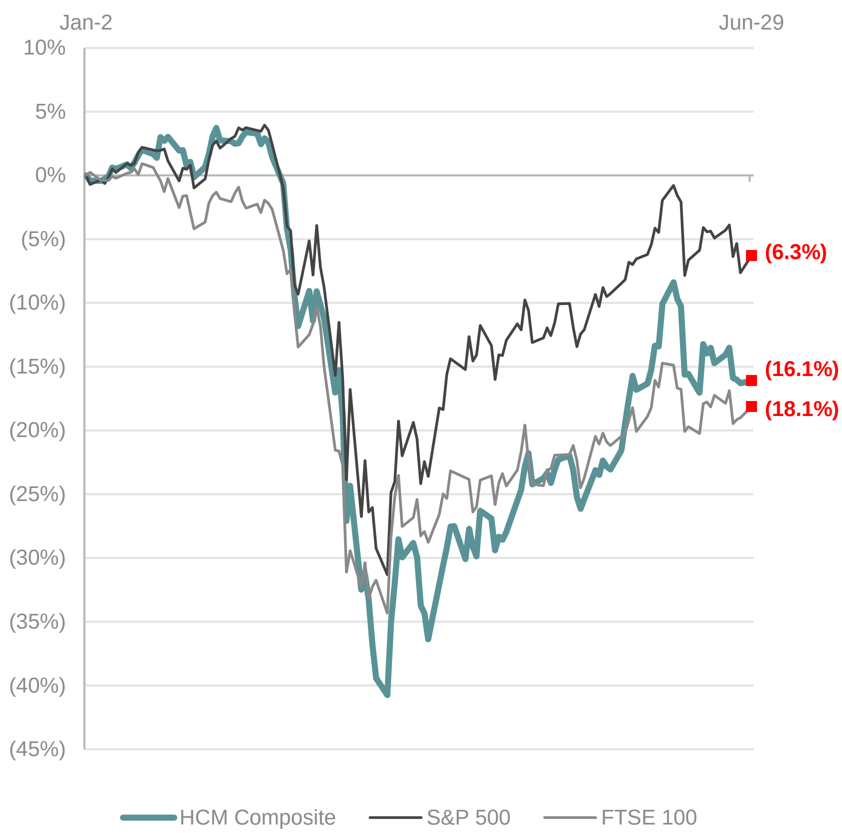
Key Topics Covered in This Update

(1) U.S. Bureau of Labor Statistics.

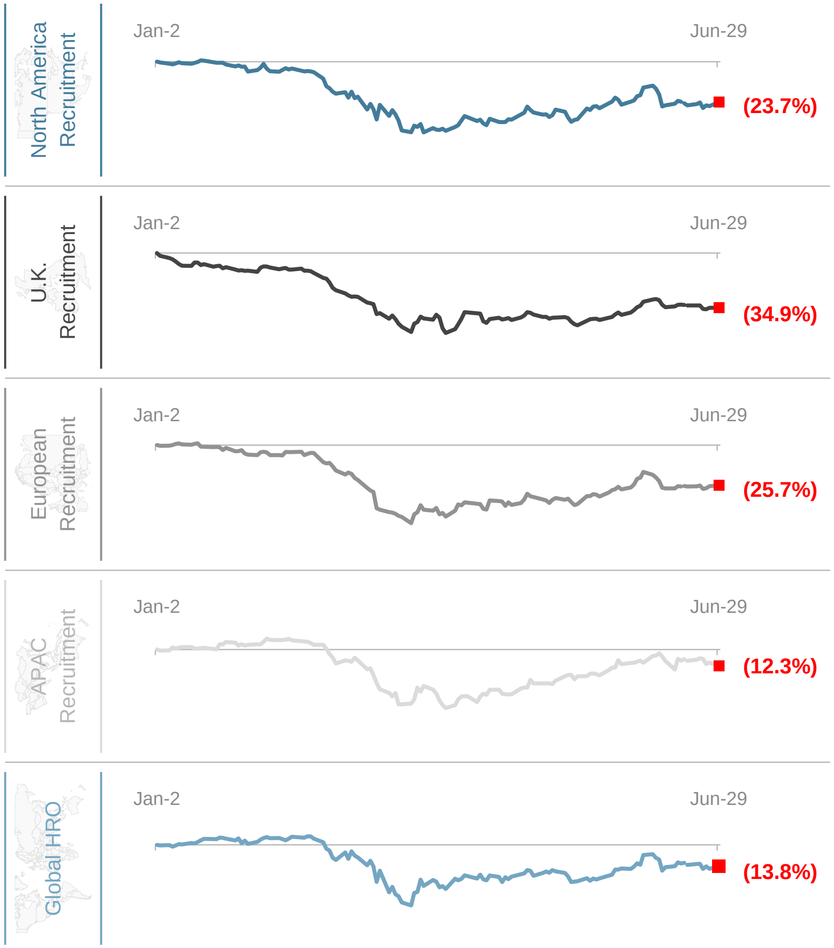
HCM Public Equity Markets: Overview of 2020 Performance

The global HCM sector has experienced considerable declines vs. the S&P 500 in the first half of 2020. However, the APAC Staffing and Recruitment and HRO/PEO subsectors have performed more favorably than the overall HCM market index.

Public Market Performance (YTD 2020)



Relative End-Market Performance (YTD 2020)

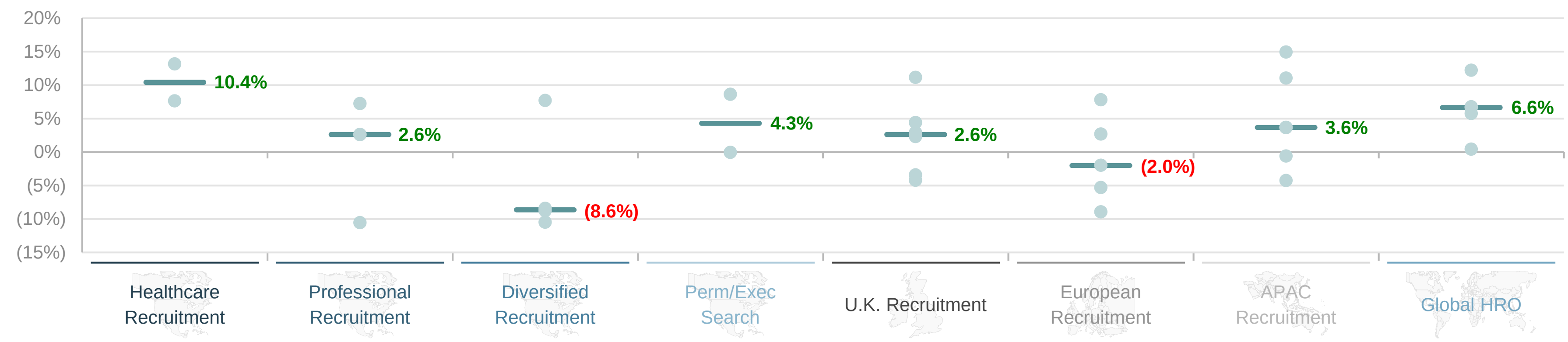


Note: North America recruitment composed of AMN Healthcare, BG Staffing, Computer Task Group, Cross Country Healthcare, Heidrick & Struggles, Kelly, Kforce, Korn Ferry, Manpower, On Assignment, Robert Half, and TrueBlue; U.K. Recruitment composed of Hays, Impellam, PageGroup, Robert Walters, Staffline and SThree; Europe recruitment composed of Adecco, Brunel, Groupe CRIT, Randstad, and Synergie; APAC Staffing and Recruitment composed of Career International, HRnetGroup, Outsourcing, Pasona, Persol, Recruit, and Technopro; Global HRO/PEO composed of ADP, BBSI, Insperity, Paychex and TriNet.

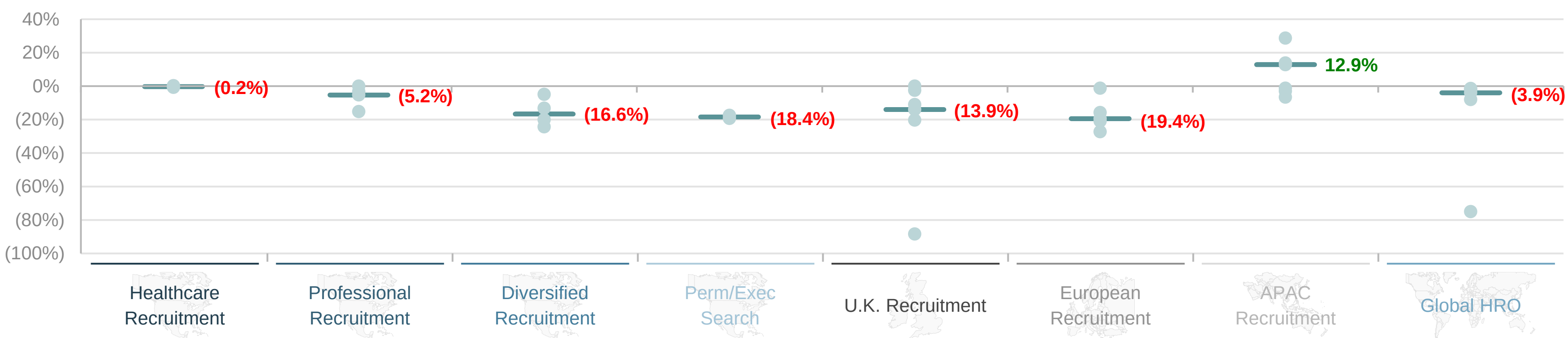
HCM Public Equity Markets: Q1 Results and 2020 Consensus Outlook

In many HCM subsectors, Q1 2020 produced modest growth year over year; however, the full-year outlook remains muted as the COVID-19 crisis continues to create a very challenging business environment.

Q1 '20 Revenue vs. Q1 '19 Revenue (% Growth)



2020E Consensus Revenue Growth Estimates (%)



Source: S&P Capital IQ.
Note: Solid horizontal line represents the median statistic within the given subsector.

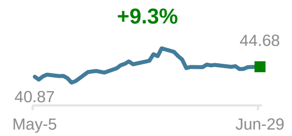
HCM Public Equity Markets: Summary of Select Q1 Earnings Data

The Adecco Group — 5/5/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(9.0%)***
- *Gross Profit* ***(8.0%)***
- *EBITDA* ***(29.7%)***

Select Analyst Commentary
- *"Although Q1 was better than anticipated and revenue is stabilizing, expect muted recovery as many furloughed staff are unlikely to begin during a recession."*

Market Response (stock price performance since earnings release)

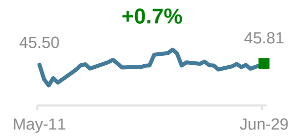


AMN Healthcare — 5/11/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***+13.2%***
- *Gross Profit* ***+14.3%***
- *EBITDA* ***+12.1%***

Select Analyst Commentary
- *"COVID-19 had positive impact on travel nursing through most of April but is expected to worsen. Management provided guidance below consensus."*

Market Response (stock price performance since earnings release)



ASGN Incorporated — 4/30/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***+7.2%***
- *Gross Profit* ***+6.4%***
- *EBITDA* ***+6.6%***

Select Analyst Commentary
- *"Anticipate ASGN to benefit from on-shoring of IT work due to its Consulting capability and assert ASGN as acquirer of choice."*

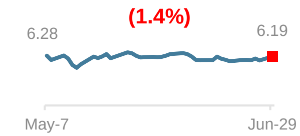
Market Response (stock price performance since earnings release)

Cross Country Healthcare — 5/7/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***+7.6%***
- *Gross Profit* ***+2.8%***
- *EBITDA* ***+27.8%***

Select Analyst Commentary
- *"COVID-19 created initial surge in demand but was offset by declines in allied and physicians. Management expects rebound in deferred treatment as economy reopens."*

Market Response (stock price performance since earnings release)

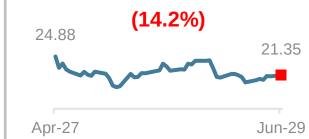


Heidrick & Struggles — 4/27/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(0.1%)***
- *Gross Profit* ***(0.8%)***
- *EBITDA* ***+14.7%***

Select Analyst Commentary
- *"Somewhat surprised HSII is maintaining headcount levels, creating medium-term profitability risk if business does not rebound to normal levels."*

Market Response (stock price performance since earnings release)

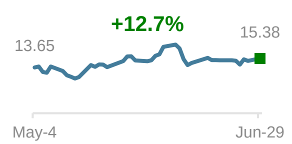


Kelly Services — 5/4/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(8.8%)***
- *Gross Profit* ***(11.2%)***
- *EBITDA* ***(25.7%)***

Select Analyst Commentary
- *"Lower demand [was] observed during the second half of March as customers react to COVID-19."*

Market Response (stock price performance since earnings release)

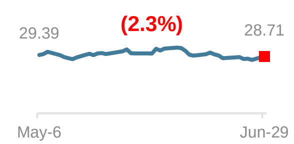


Kforce — 5/6/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***+2.6%***
- *Gross Profit* ***+1.4%***
- *EBITDA* ***+1.6%***

Select Analyst Commentary
- *"The strategic decision to consolidate share in higher-end domestic IT staffing provides resilient demand for KFRC in challenging business environments."*

Market Response (stock price performance since earnings release)



ManpowerGroup — 4/21/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(8.4%)***
- *Gross Profit* ***(10.0%)***
- *EBITDA* ***(37.5%)***

Select Analyst Commentary
- *"Severe declines since late Q1 '20 but strong business mix should better position MAN; April could be [a] low point, depending on [the] timing of reopenings."*

Market Response (stock price performance since earnings release)

Randstad — 4/22/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(5.3%)***
- *Gross Profit* ***(7.0%)***
- *EBITDA* ***(33.8%)***

Select Analyst Commentary
- *"Reported better-than-expected Q1 results and is trading at trough multiples; expect temporary staffing to benefit from sustained downturn."*

Market Response (stock price performance since earnings release)

TrueBlue — 5/4/20 Release

Performance/Q1 Results (% YoY)
- *Revenue* ***(10.5%)***
- *Gross Profit* ***(14.0%)***
- *EBITDA* ***(72.6%)***

Select Analyst Commentary
- *"Significant drop in demand began in the second half of March, so management is reducing expenses by $100 million this year; no guidance [was] provided."*

Market Response (stock price performance since earnings release)

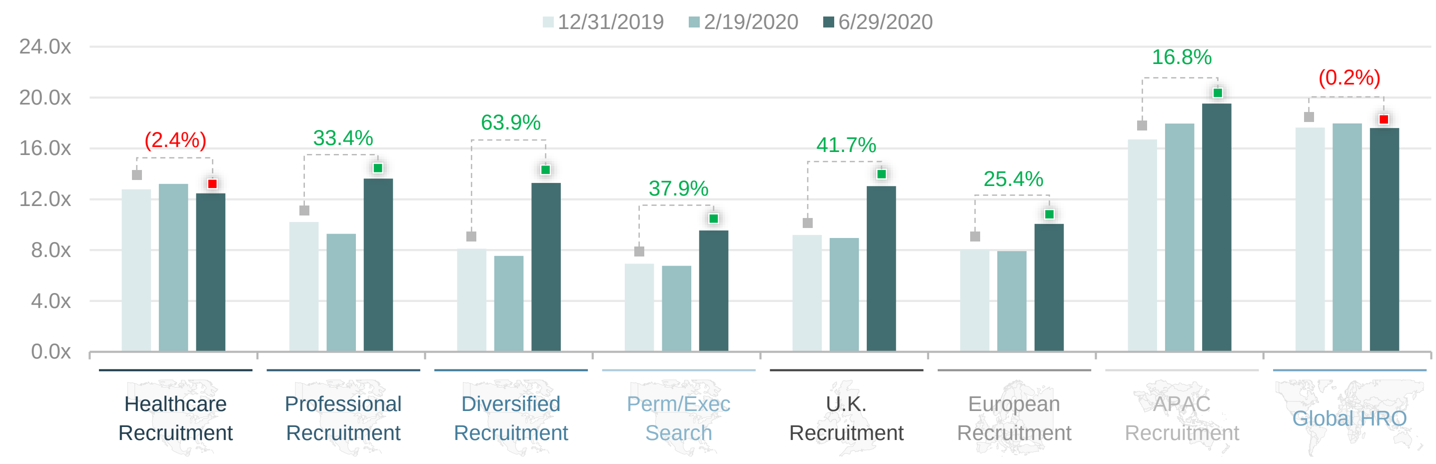
Source: S&P Capital IQ and public filings.

HCM Public Equity Markets: Impact of COVID-19 by Subsector

Macroeconomic uncertainty related to COVID-19 has severely impacted valuations for many public HCM firms. Houlihan Lokey's global HCM index of 35 firms is down 16.1% since the beginning of the year and 18.5% since the onset of COVID-19-related market volatility (February 19).

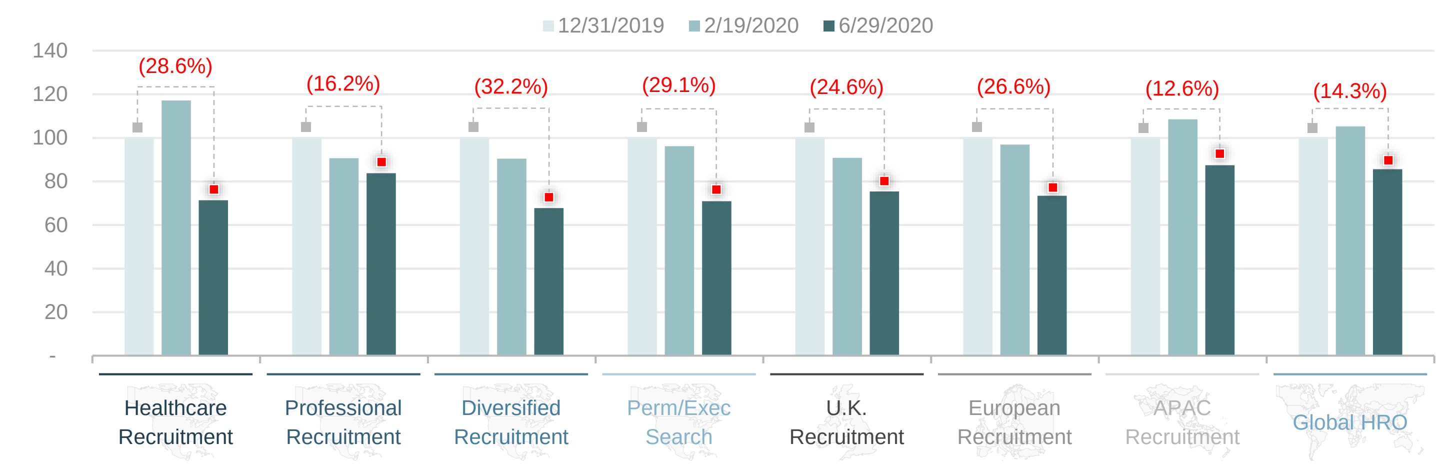
EV/NTM EBITDA Multiples

Across most subsectors of the global HCM universe, forward public EBITDA multiples have increased during the COVID-19 market dislocation, providing a boost to otherwise declining valuations (see below).



Equity Valuation (Indexed)

Despite strong Q1 financial results, public equity valuations were slightly down through January and February 2020, with the market impact of COVID-19 in late February causing further deterioration across all HCM subsectors.



Source: S&P Capital IQ.

HCM Public Equity Markets: Impact of COVID-19 by Subsector (cont.)

While valuations have declined, a closer look reveals that multiples are still relatively healthy, and lowered consensus EBITDA estimates are the biggest contributor to the decline, implying the potential for a speedy recovery once forecasts turn positive.

Decline in Public HCM Valuations Due Primarily to Lower NTM Earnings vs. Multiple "Re-Rating"

Public HCM indices across all subsectors have declined since the beginning of 2020, and in almost all cases, revised downward NTM earnings expectations have been the primary driver of value erosion.

In seven of the eight subsectors, strengthening forward multiples helped boost valuations above the much lower floor implied by underlying earnings.

The collective resilience of public HCM multiples is a positive sign for sector valuations when economic growth returns.

Source: S&P Capital IQ.
Note: Positive percentages reflect impact (positive or negative) from i) revised earnings or ii) changes in the forward trading multiple that are in line with the positive or negative change in market cap/equity value (e.g., lower consensus earnings as a positive percentage explanation for subsectors showing declining valuation) and vice versa.

Themes from the HCM Executive Suite

Over the last few months, Houlihan Lokey's HCM team has held hundreds of discussions with founders, owners, executives, and investors across the HCM landscape. While circumstances vary by geography, solution, and specialty, certain themes have been consistently highlighted by executives and investors across staffing, VMS/MSP, RPO, and direct hire/search.

Summary Views on Business Performance

I Lenders, somewhat cooperative and flexible through Q1 covenant compliance, have been increasingly less so in Q2 given tepid financial performance (uncertain outlook for Q2 reactions).

II There is significant variance in COVID-19 impact by specialty, with IT performing better (~5% growth to ~5% decline) than other skills (e.g., finance and accounting down ~20%, industrial down ~40%–60%, etc.).

III While down year over year, the rate of decline slowed or stopped for many in May and June. After "bumping along the bottom" in early May, reports of slow increases in late May and June are increasingly common.

IV As hospital budgets and cash flows are strained due to a lack of elective procedures, healthcare staffing firms are reporting increased difficulty after a nice spike early in the pandemic.

Summary Views on Customers and Operations

I Cuts to internal FTEs are more widespread, especially outside of IT, although focus has been in many cases on bottom performers in order to maintain productive capacity for a market upswing.

II As businesses begin to reopen, executives are struggling to navigate compliance with health mandates under the reality of in-person work (e.g., maintaining social distance at a job site, availability of Paycheck Protection Program).

III While a handful of clients have requested revised or extended payment terms, federal programs supporting liquidity have kept bad debt from being a widespread issue to date.

IV While the work-from-home shift has been seamless for the majority of firms, logistical challenges with a client's ability to remotely deploy headcount remain common.

Managing Liquidity and Revenue Declines

HCM firms can expect erratic changes in customer behavior due to COVID-19, with the added difficulty of managing such change amid the uncertainty of a temporary response to a cyclical downturn or something more permanent. In this environment, immediate bold action on liability, cash, and revenue management will leave firms better positioned to navigate the current downturn and to successfully position themselves for growth when the market inevitably rebounds.

Establish a Senior Battle Team

- Many companies are appointing a senior, fully dedicated COVID-19 specialist team internally that is dedicated to the effort.
- In addition to staying updated on the various health and related aspects of the virus, alongside the CEO, they are proactively managing and thinking through strategies.

Cash Is King

- A deep understanding of your cash and working capital requirements are critical, especially as it pertains to understanding your borrowing base and avoiding potential covenant breaches.
- Approaching lenders, landlords, and other creditors proactively helps to add stability around some of the more volatile and onerous aspects of your expense base.

Forecast Your Exposure

- Modeling out financial performance scenarios, with specific detail around customer performance and potential payment delays, is an important exercise and conveys confidence to lenders.
- Given the unique uncertainty of the current situation, stress testing the scenarios and including "extreme" cases will help prepare for various outcomes.

Evolving Working Capital

- Stress testing your working capital needs for upcoming swings in days payable and days sales outstanding can avoid future surprises.
- As customers extend payments or defer to the future, timing is paramount for this exercise.
- It is critical to also model post-crisis growth and understand future liquidity impact during a quick market recovery.

Frequent Contact with Lenders

- The "partnership" concept that lenders espoused when times were good will come into play.
- Although your lender knows your business, the transparency, frequency, and even tone of your discussions can have a meaningful impact and material influence on the lender's flexibility in many situations, which might arise in the months ahead.

Proactively Manage Declines

- Review your business outlook in detail, and focus attention on revenue and a profitability mix of specific customers and segments.
- Use this opportunity to pivot and reallocate resources to emerging pockets of growth.

Planning and Preparing for a Recovery: Overview of Financing Alternatives

Having relied on significant liquidity to manage the COVID-19 downturn, many HCM firms will face unique funding challenges as the market recovers and they return to growth mode. Substantial "dry powder" from nontraditional funding sources is available to fill a variety of unique needs (e.g., liquidity assistance to fund working capital, bridge financing to help manage temporary funding shortfalls, merger and acquisition financing for strategic M&A, etc.).

Financing Market Update

- While capital availability is currently limited for new leveraged buyout (LBO) transactions, the markets are open to support liquidity needs of company issuers navigating the uncertainty.
- Financing can take the form of debt, equity, or a hybrid involving a convertible security.
- Capital providers include both lenders as well as traditional buyout firms eager to put capital to work, even if in a minority equity or debt security.
- Opportunistic capital providers are looking for good companies with bad balance sheets and differentiated and defensible platforms.
- Direct lenders have continued to prepare for what they believe will be a wave of distressed debt and unique financing opportunities. KKR recently raised ~$4 billion in capital to support its dislocation credit strategy and invest in opportunities created by recent market volatility.
- While M&A activity has slowed and traditional lending options are unreliable, opportunistic M&A deals arising in the future might require the support of structured capital solutions to close (e.g., stock for stock, structured equity, seller paper, bridge financing, etc.).

Overview of Unique Capital Providers

Private Equity

- More hands-on; capital and operational value
- May or may not seek path to eventual control
- Would seek ~40% equity ownership with commensurate board representation
- Typically require seniority to existing investors and will invest as convertible preferred stock

Structured Equity Fund

- Less hands-on; passive investors requiring fewer governance rights and limited board representation
- Would seek to own approximately ~15%; security typically preferred stock with penny warrants
- Ability to move quickly to close on capital solution

Debt Investor

- Management and board free to set strategic direction
- Limited or no equity dilution (some may require modest warrants)
- Requires certain covenants and debt service obligations (interest expense, principal repayment)

How Houlihan Lokey Can Help

Our firm is extremely well-equipped to help our clients navigate uncertain times. We respond quickly to challenging situations and are constantly helping clients to analyze, structure, negotiate, and execute the best possible solutions from both a strategic and financial perspective.

What We Offer

1 Corporate Finance

We are widely recognized as a leading M&A advisor to the middle market and have long-standing relationships with capital providers, including commercial banks and other senior credit providers, insurance funds, asset managers, and mezzanine fund investors. Few other investment banks maintain the breadth of relationships and capital markets intelligence that we do.

- Mergers and Acquisitions
- Capital Markets
- Special Situations M&A and Financing
- Private Funds Advisory
- Board Advisory Services

2 Financial Restructuring

We have the largest restructuring practice of any global investment bank. Since 1988, we have advised on more than 1,000 restructuring transactions with aggregate debt claims in excess of $2.5 trillion. We served as an advisor in 12 of the 15 largest corporate bankruptcies from 2000 to 2019.

- Company Advisory
  - Financial Restructuring
  - Distressed M&A
  - Liability Management
- Creditor Advisory

3 Financial and Valuation Advisory

For nearly four decades, we have established ourselves as one of the largest financial and valuation advisory firms. Our transaction expertise and leadership in the field of valuation helps inspire confidence in financial executives, boards of directors, special committees, investors, and business owners we serve.

- Portfolio Valuation and Fund Advisory
- Transaction Opinions
- Corporate Valuation Advisory Services
- Transaction Advisory Services
- Real Estate Valuation and Advisory
- Dispute Resolution Consulting

Houlihan Lokey's Dedicated HCM Team

Our team is one of the most active and experienced HCM groups on Wall Street.

Human Capital Management Team

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2014 All U	2015 All U	2017 All U	2018 All U
1	1	1	1
1	2	2	2
1	2	2	3*
4	2	4	3*
5	5	4	5
5			

2019 M&A Advisory Rankings
All U.S. Business Services Transactions

	Advisor	Deals
1	HOULIHAN LOKEY	24
2	Raymond James Financial Inc	13
2	Lincoln International	13
4	Generational Equity	12
5	William Blair & Co	10

Source: Refinitiv (formerly known as Thomson Reuters)

- In 2019, HL was the most active Business Services M&A advisor in the U.S. and closed a total of 24 deals.
- We have been the No. 1 Business Services M&A advisor for the past five years, and we have the transaction experience and expertise to provide industry-leading advisory for any client.

HCM

Select Human Capital Management Transactions

- TrustHCS, a portfolio company of WindRose, has been acquired by a joint venture of The Carlyle Group / Cannae — Sellside Advisor
- Avedon Capital Partners has sold its majority stake in Olympia to Management and Morgan Stanley Investment Management — Sellside Advisor
- ettain group, a portfolio company of NMS Capital, has been acquired by A&M Capital Partners — Sellside Advisor
- Global Employment Solutions, a portfolio company of TZP, has been acquired by ettain group, a portfolio company of A&M Capital Partners — Sellside Advisor
- CDI Corporation, a portfolio company of ae Industrial Partners, has divested MRINetwork to Bert Miller — Sellside Advisor
- ingeus, the Workforce Development Services division of Providence Service Corporation, has been acquired by APM — Sellside Advisor
- Eliassen Group, a portfolio company of Riverside Partners, has been acquired by Stone Point Capital — Sellside Advisor
- CDI Corporation, a portfolio company of ae Industrial Partners, has divested CDI Talent & Technology Solutions to Artech — Sellside Advisor
- TP★GS has been acquired by system|one, a portfolio company of Thomas H. Lee Partners — Sellside Advisor
- Motion Recruitment, a portfolio company of Gridiron Capital, has been acquired by Littlejohn & Co. — Sellside Advisor
- MedPartners has been acquired by AMN Healthcare — Sellside Advisor
- ECS along with minority investor Lindsay Goldberg has sold ECS Federal to On Assignment — Sellside Advisor
- FFL Partners has completed a majority investment in ProService Hawaii — Buyside Advisor
- CDI Corporation has been acquired by ae Industrial Partners — Sellside Advisor & Fairness Opinion
- CIP Capital has made a strategic investment in WilsonHCG — Buyside Advisor
- Principle Solutions Group has partnered with Eliassen Group, a portfolio company of Riverside Partners — Sellside Advisor
- ciber has been acquired by HTC global services — Sellside Advisor
- search, a portfolio company of Chamonix, has been acquired by H2 Equity Partners — Sellside Advisor
- ICS Independent Clinical Services, a portfolio company of Towerbrook, has successfully completed a dividend recapitalisation — Financing Advisor
- ciber Infor Practice, a subsidiary of ciber, has been acquired by infor — Sellside Advisor
- ciber Spain, a subsidiary of ciber, has been acquired by ManpowerGroup — Sellside Advisor
- PAN has been acquired by psi — Sellside Advisor
- ABN AMRO Participaties has sold HumaRes to bencis capital partners — Sellside Advisor
- system|one, a portfolio company of MidOcean Partners, has been acquired by Thomas H. Lee Partners — Sellside Advisor
- Bond Recruitment Software, a subsidiary of Bond, has been acquired by symphony — Sellside Advisor
- hr&payroll software, a subsidiary of Bond, has been acquired by Tenzing — Sellside Advisor
- CAPS, a portfolio company of Unsworld Capital, has been acquired by Cash & Crew, a portfolio company of SilverLake — Sellside Advisor

Note: Tombstones included herein represent transactions closed from 2016 forward.

HOULIHAN LOKEY

CORPORATE FINANCE

FINANCIAL RESTRUCTURING

FINANCIAL AND VALUATION ADVISORY

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