

DISRUPTION IN STAFFING

Sector-by-sector predictions of market share impacts from the Human Cloud.

How each staffing niche can respond with M&A to survive and succeed.

the l

STORM CLOUDS AHEAD . . .

Human Cloud headed to change recruitment dramatically

The Human Cloud is going to have a dramatic impact on the staffing industry. It's not just that the technology will respond better to increasing employer and candidate demands, but the addition of AI, blockchain and other innovations will make the Human Cloud more effective still.

The staffing industry is talking about this disruption. The conventional wisdom is to view it an inevitable force that will sweep across the sector where the primary question is how fast and deep the disruption will cut.

In fact, the more practical question is which staffing sub-sectors will be impacted when – because the prognosis for each will be so different.

The other question is what staffing companies should do about it – wait for the tsunami, as many are doing, or take action to either get out of the way or ride the wave.

M&A – whether to position oneself actively to win or defensively with an exit plan before it's too late – warrants immediate consideration.

Purpose of report

The absence of a clear view in the market forces people into denial or delay. The general growth of the Human Cloud and individual success stories popping up doesn't give much guidance to individual businesses.

The purpose of this report is to open that debate and provide insight, evaluation and strategy where it is needed – at the sub-sector level – and what can be done to survive or succeed, but at all costs not get squashed.

The future will be a very different world, quite soon, but what will it look like? Disruption will hit different niches at different times and to differing degrees.

There is little to no predictive data on the Human Cloud trend and specifically its disruptive impact on staffing.

Therefore, we have set out to provide this, and, by using our sector knowledge, to peel apart the ingredients of disruption and apply them to recruitment niches to predict what may happen.

The cornerstone of this effort is the building of a 'Disruption Database' covering the 80 key staffing sub-sectors.

This allows us to see what will likely happen to revenues, margins, EBITDA and valuation multiples of different segments who remain wedded to traditional staffing.

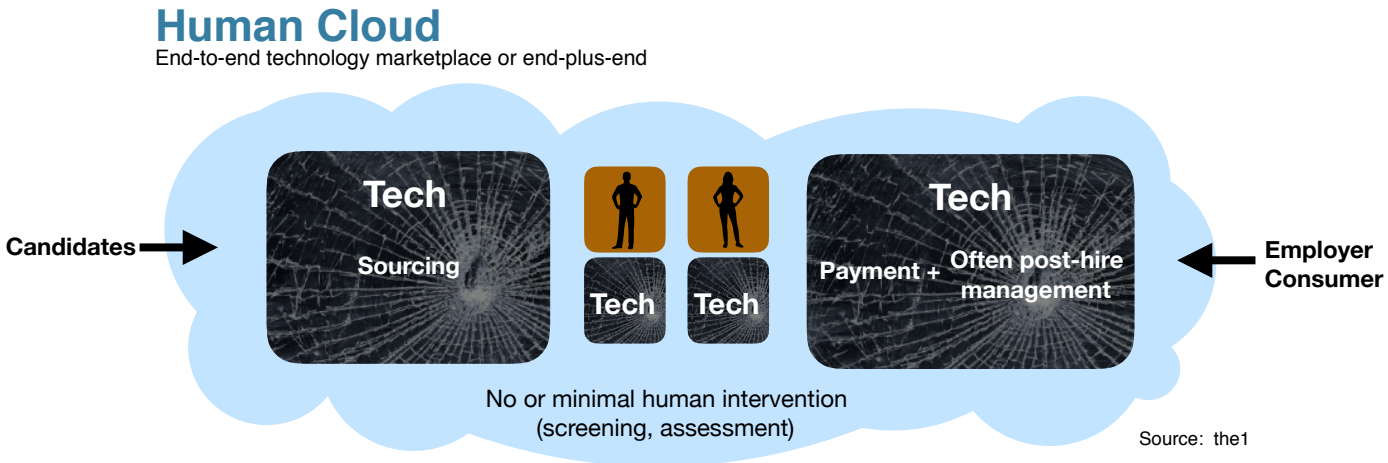
Human Cloud vs. HR Tech

The Human Cloud for us means a technology interface at both the candidate and customer end. Even if there is staffing intervention going on in between the two facades, it is still Human Cloud. When the customer is served with a technology interface but the candidate or temp worker is sourced and integrated in a traditional way, we call it 'Half Cloud'.

The myriad of individual HR technologies, by contrast, which employers and the staffing industry are deploying to be more competitive, is outside our definition. Indeed, almost every staffing business has or will embrace up to dozens of specific technologies whether home-grown or licensed.

The staffing or human capital sectors that are not offering Human Cloud are considered by us by contrast to be 'Human Earth' businesses, regardless of how much technology they use as long as it doesn't reach the definition of a Human Cloud marketplace type business. This allows us to draw a clear line between earth and cloud which is currently fuzzy in the market.

This report looks at the impact Human Cloud businesses will have on Human Earth businesses, notwithstanding that within the Human Earth space there will be winners and losers based how successfully they adopt and deploy HR tech. This is a quite separate issue.



Source: the1

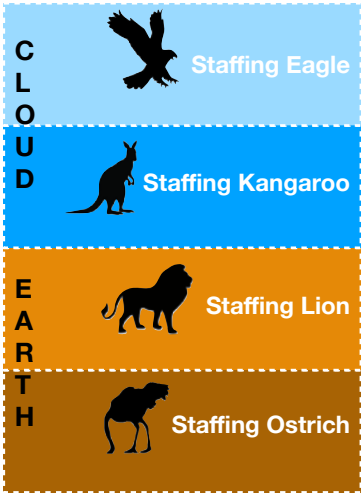
. . . AND A NEW LANDSCAPE WILL RESULT

Pointing upwards

At the very bottom of the technology space are staffing companies doing little to nothing with technology or only paying lip service to it. We call them 'staffing ostriches' because they have their heads in the sand.

The next slice of Human Earth covers progressive staffing companies which will capture market share from the laggards while winning in a declining Human Earth space. They may feel like they are rising but are rising in a falling tide as their market shrinks. We call them 'staffing lions' because the will rule the earth but ultimately will never take off.

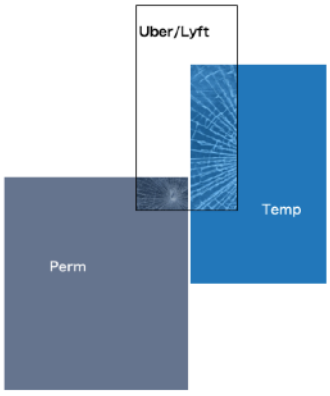
From Earth to Sky
Rising to the challenge



As we move up into the lower atmosphere we see staffing companies which are involved in Human Cloud but as partners with actual Human Cloud businesses which own the technology and control the brand or at least the master brand, such as the relationship True Blue and TalentBurst have with Uber. If these companies don't view such agreements as stepping stones they will see their margins squeezed as the brand-owner's momentum gives it an increasing share of the gross profit of the transaction revenues. We call them 'staffing kangaroos' because they are making an earnest attempt to fly but they are doomed to come down to reality unless they change their game.

Finally, some companies will rise to the stratosphere where true Human Cloud enjoys natural monopoly economics and valuations. This will be the world in which the eBay's and Uber's of the human capital sector are created, players like Upwork, MBO Partners, Gerson Lehman, Fiverr and Axiom. These are the 'staffing eagles' which will dominate the Human Cloud.

New white space
Invisible disruption



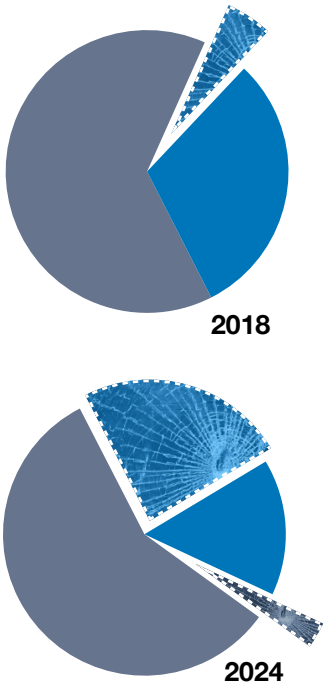
Disruption

Human Cloud business models often look so different from traditional ones that their disruptive impact may be underestimated.

That said, the disruption doesn't have to come solely at the expense of Human Earth. Human Cloud will change the way workers find jobs beyond the sector, placing people who are currently hired directly by employers and in that sense will expand the overall cake. Put another way, the workers and revenues passing through Human Earth and Human Cloud combined will be greater than they are today.

Also, just because Human Cloud will operate most successfully among temporary workers doesn't mean it will only disrupt 'Temp Human Earth'. 'Perm Human Earth' headcount will evaporate to the cloud where it will become 'Temp Human Cloud' rather than 'Perm Human Cloud'. Put another way, just because we will see very little Perm Human Cloud business in the next five years, Perm Human Earth will still shrink dramatically.

Temp Disruption won't be temporary
The impact on temp and perm



Source: the1

Nevertheless, the largest bite will come from Temp Human Earth cutting it approximately in half of what it is today but, because of the bite from perm, growing to more than double.

The decline of Temp Human Earth will counterintuitively coincide with a huge growth in the total temp market when Earth and Cloud are combined.

The context of a fairly stable working population means that these tectonic dynamics will result in extraordinary impact on the overall size of the Human Earth sectors, whether perm or temp. Any large and diversified business operating in this space can expect to see its revenues collapse if it treads water. Niches will suffer different degrees of disruption and some may, at least in the medium term, not have to face extreme disruption.

BAROMETERS OF CHANGE

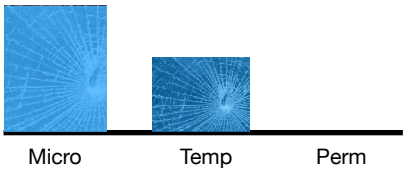
Key disruption drivers

Disruption obviously doesn't just happen. It will be the result of how technology interplays with candidates' and employers' needs. Its impact will be very uneven across different staffing sub-sectors.

The devil is in the detail. To predict where disruption will be felt, how strongly, and when, we have identified six key ingredients or 'drivers of disruption' from the Human Cloud.

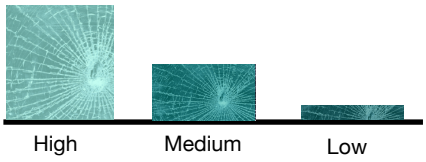
They are: the duration of employment (whether from a micro assignment, temp or perm); the internet proficiency of the typical candidate base, which is often but not always correlated with age; the pay rate; the need or willingness of worker or employer to offer flexibility in working hours; how remotely the task can be managed and how eager the candidate is for remote work; and the level of commitment involved in the work, whether full-time or part-time.

Duration



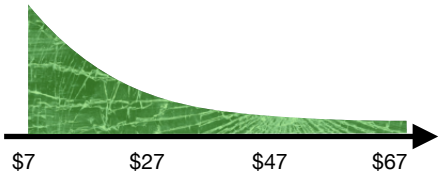
Currently perm isn't effect by Human Cloud as precisely defined. The substantial employer commitment requires more need for human intervention and cultural fit than the Cloud is able to cope with. However, with the speed of AI development it could be possible that a small slice of the perm positions could be filled by Human Cloud in five years. Failing that, the furthest perm will go will be to a Tinder model (ie not to the hire point) rather than to an Upwork model.

Internet proficiency/ age



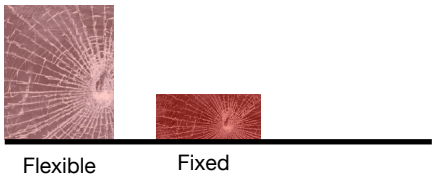
People with higher internet proficiency (broadly speaking younger people) are more likely to insist on the Human Cloud as a way to find jobs compared to older people. In general there are more younger workers in the entry-level and junior roles versus older people at the higher. Therefore in our sub-sector analysis we classify management/ C-level roles as medium/low impact in this dimension.

Hourly rate



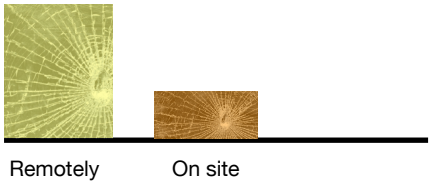
Globally almost all freelance workers fall into the hourly pay range $11-$28 (per Payoneer survey 2018), meaning they will all be in high impact territory. Most freelancers recruited through the Cloud are in the logistics & hospitality industries at the lower payment range. An increasing number of Human Cloud operator are targeting freelancers in higher paid space such as design, IT and marketing. The Cloud is moving up the food chain but will sweep lower levels more fully.

Flexibility of hours



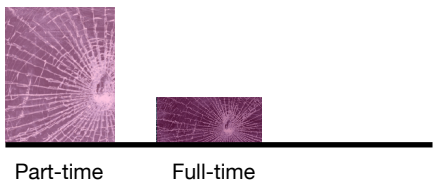
The variety of working hour flexibility of jobs on the Human Cloud allows workers to choose when they want to work. Indeed, flexibility is the top reason for many people who started doing gig or freelance work and one of the top reasons employers use the Cloud to hire short-term or on-demand workers, to address the employers' need at short notice. The Cloud will dominate positions with flexible working hours.

Managed proximity



In addition to flexible hours, Human Cloud offers more flexibility in work location. Remote projects are taken up by people who source them through Human Cloud, while employers benefit from managing remote workers directly through the Cloud hassle-free. Therefore the Cloud will play a more vital role in remote work than on-site work which can be managed with less technology.

Commitment



With the ease of hire and time management offered by Human Cloud, part-time roles in the future will develop into even shorter commitments allowing a person to work for more employers or on multiple projects at the same time. Such benefit is less useful in full-time roles.

Some of the themes which interplay with the six drivers are the need for human intervention and what is critical for candidates or clients.

Each of the fundamental six drivers of disruption is a different dimension in the sense that any type of recruitment can be classified by the six measures to describe the business model more fully, as opposed to other factors such as job function, sector and geography. Since every staffing business is made up of these dimensions, the propensity of each to disruption by the Human Cloud will combine to determine the extent and timing of the disruption.

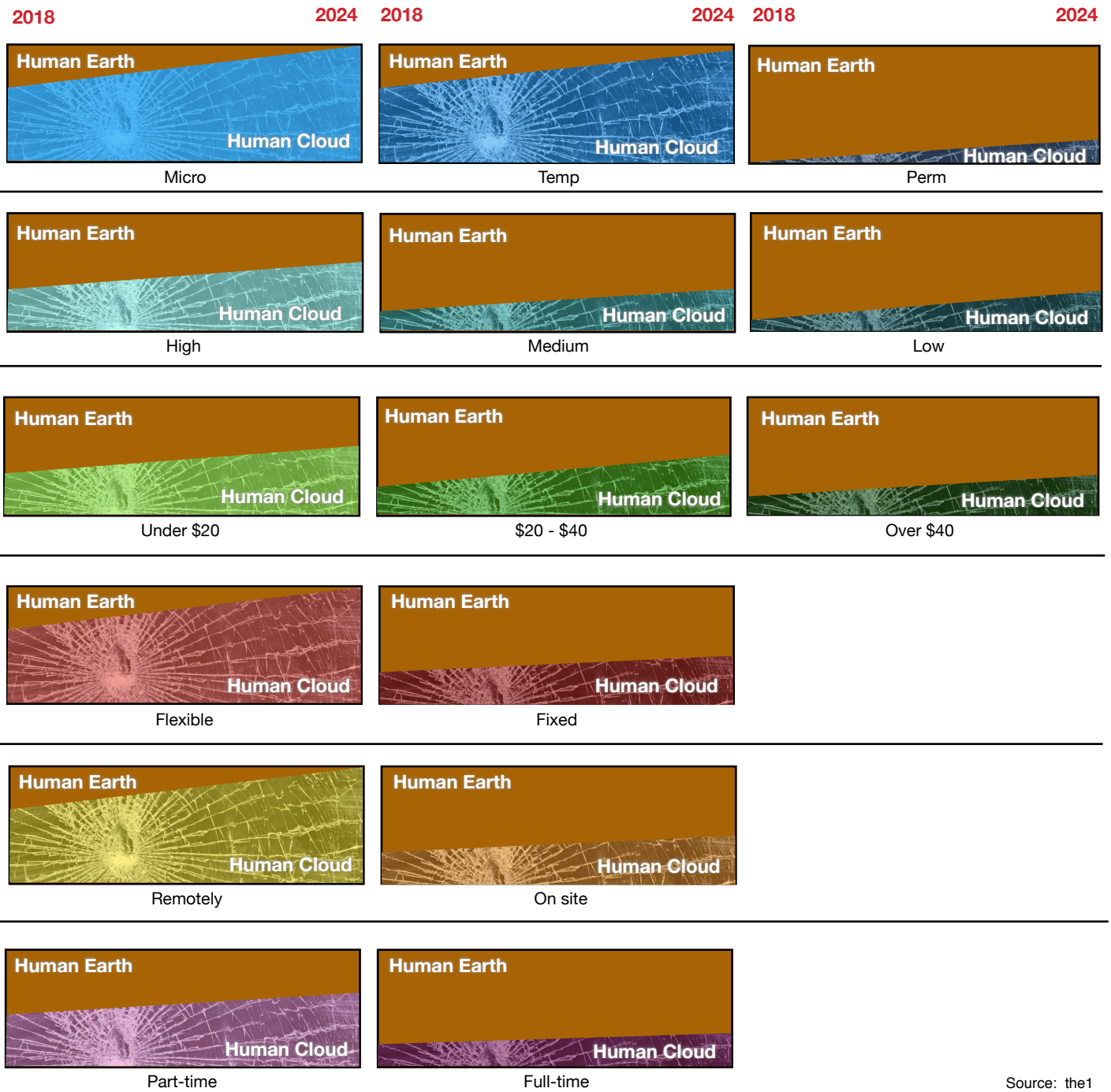
They conspire together for each type of business and indicate what can be expected to happen.

How the drivers will heat up

Each of these can be viewed as 'disruption barometers' each with its own prognosis.

Having identified these drivers, we can look at how the different components of each are likely to be effected by the Human Cloud over the next five years to see what is in store for each barometer.

This in turn allows us to look at any particular staffing sector niche, identify where it sits on the spectrum for each driver and then apply what is likely to happen to that driver or barometer in the future to give a balanced six-dimensional predictive view.



Source: the1

Sub-sector prophesies

Having identified and measured the trajectories of the six 'drivers of disruption', we are now in a position of having the trajectory projections of these barometers at hand to analyse each staffing industry sub-sector. With this detail it's possible to look at the impact of the Human Cloud on individual niches within the Human Earth as opposed to just the overall landscape.

A to Z of disruption impact by temporary staffing sub-sector

		A&F - Interns				A&F - Junior T	
		Classification	Comment	Impact		Classification	Comment
Disruption level by dimension	Duration	Temp	–	High impact		Temp	–
	Internet proficiency / age	High	–	High impact		High	–
	Hourly rate	Low	–	High impact because low risk to employer		Low	–
	Flexibility of hours	Fixed	Cloud technology might bring expand flexibility	Medium impact		Fixed	Cloud technology might bring expand flexibility
	Managed proximity	Onsite	Onsite tradition to be disrupted to allow remote cross-border interns	High impact		Onsite	Combination of E-accounting and Cloud allows remote
	Commitment ((p/t or f-t)	Half or full-time	Allows even shorter commitment to allow 2-3 internships	High impact		Half or full-time	Allows even shorter commitn to allow 2-3 jobs
Disruption analysis	Worker change	Would enjoy speed of decision, amortising of video CV effort in finding jobs and increased flexibility of work hours, potential for more lower commitment internships in parallel, and generally would be conversant with online platforms. 10-country 10-internship grads could be imagined on a CV.				Would enjoy speed of decision without the need to deal with s hours, potential for lower commitment contract work in parall online platforms.	
	Employer change	Would benefit from streamlined hiring and would be willing to take risk of hiring without f2f. At work, would benefit from scheduling flexibility when needing more or less support.				Would benefit from streamlined hiring directly through Human getting more control on who they hire while keeping the proce benefit from scheduling flexibility when needing more or less	
	Conclusion	Major impact. It's attractive to both parties. However some employers and even some interns will insist on f2f to avoid cultural misfits etc but the advantages of Cloud outweigh even that factor.				Major impact. It's attractive to both parties. This huge staffin	
the1 Shock Factor	Cloud mkt share 2019	0%				3%	
	Cloud mkt share 2024	53%				49%	
the1 Disruption Degree		EXTREME				EXTREME	

Realities facing sector

Natural monopoly

The Human Cloud is a natural monopoly which of course means it's either an opportunity or a threat depending on which side you end up on.

The key barrier to entry is achieving sufficient momentum – of enough buyers and sellers, as in any marketplace business – to kickstart the marketplace. This 'catch 22' polarises users between disappointment and satisfaction. A staffing company may be able to break the impasse by 'priming the pump' through the creation of what can be called a 'simulated cloud' out of the company's existing clients and temp workers, rather than relying on fresh clients and candidates at the outset. This 'simulated cloud' can then develop into a 'sustainable cloud' business which then benefits from the marketplace's momentum.

These dynamics are very different from the way a traditional staffing business grows because, at the point of success in Human Cloud, customers and candidates both come in because marketplace works, with critical mass success then attracting both categories away from alternative businesses, whether Human Capital or Human Earth.

Customers and candidates save time by reducing the number of marketplaces or providers they need to participate in which further polarises the market in favour of one monopolist. Finally, the leading marketplace also grows by user word-of-mouth in the way Uber and eBay did, which further drives out smaller competitors who have to pay for users at either or both ends of their Clouds.

Patchwork monopolies

The Human Cloud natural monopolies won't necessarily evolve globally or across all niches. 'Safe zones' will be formed by micro barriers to entry, primarily because of:

- proximity between candidates and customers, such as in a particular city, which may act as a barrier even to a powerful brand outside.

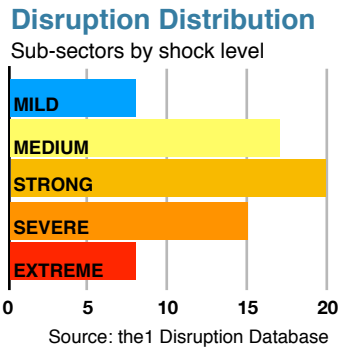
- affinity in a professional community with a mix of reputation and relevant content will likewise erect a barrier.

When a business has both of these factors working for it, the barriers are especially high. Indeed, companies can benefit from a classic 'and/or quadrant': geographical barrier; professional barrier; both; neither, where the double

Using this approach, we were able to construct the1's Disruption Database, where each sub-sector shows a different future based on how the six dimensions impact it. We see that some are going 'suffer' in disruption terms from all of the six disruption stars aligning, while others enjoy a low combined disruption from all six, while most sub-sectors will suffer impact between these extremes.

The analysis brings each niche down to a sub-sector disruption percentage which will call 'Shock Factor' and a classification of impact level which we call 'Disruption Degree'.

Not unexpectedly, most niches are expected to experience 'medium', 'strong' and 'severe' disruptions with a minority in two tails of the bell curve, 'mild' and 'extreme'.



Source: the1 Disruption Database

Temps		A&F - Temporary CFOs			A&F - Interim CFOs		
	Impact	Classification	Comment	Impact	Classification	Comment	Impact
	High impact	Temp	–	High impact	Temp	–	Highly impact
	High impact	Medium-low	–	Medium/low impact	Medium-low	–	Medium/low impact
	High impact because low risk to employer	High	–	Low impact due to high risk for employer at a C-level	High	–	Low impact due to high risk for employer at a C-level
g	Medium impact	Flexible	The positions are inherently flexible and could be booked with tech	High impact	Fixed	–	Low impact
g	High impact	Onsite or remote	Combination of E-accounting and Cloud allows remote	High impact	Onsite or partly remote	Combination of E-accounting and Cloud allows remote	High impact
ment	High impact	Part-time	Allows even shorter commitment to allow working for more employers	High impact	Full-time	–	Low impact
staffing cos and increased flexibility of work el, and generally would be conversant with		Would enjoy the flexibility and precise control for allocating different time slots to different employers they work for, therefore enables them to work for more employers at the same time while keeping the schedule well-organised.			Would enjoy the ease of Human Cloud for sourcing. The management system embedded in Human Cloud also would make it easier for CFOs to work partly remotely even when they are full-time.		
Cloud, rather than through a staffing co, ess simple and speedy. At work, would support.		Would benefit from streamlined CFO research/hire and 'booking' process provided by the Cloud. Would be able to manage more flexible working hours and address their on-demand need of an CFO at shorter notice.			Would benefit from streamlined CFO research and hire process provided by the Cloud, saving time.		
g sub-sector will be transformed.		It's theoretically beneficial for both sides, especially since the nature of the work of a CFO might not require high-level cultural fit despite this being at C-level. However due to the high pay rate of C-level people and the critical role, many employers will still be afraid fo the Cloud replacing f2f meetings. This factor may act as a veto despite many others being disruptively positive.			It's theoretically beneficial for both sides, especially since the nature of the work of a CFO might not require high-level cultural fit despite this being at C-level. However due to the high pay rate of C-level people and the critical role and full-time interim position, most employers will be afraid fo the Cloud replacing f2f meetings. This factor is expected to act as a strong veto of transition to the Cloud.		
		0%			0%		
		9%			3%		
E		MILD-MEDIUM			MILD		

Source: the1 Disruption Database

M&A STRATEGIES TO RESPOND

protection of course is best. For example, a Human Cloud business focused on Singapore dual language interim CFOs might be very well-protected whereas a US national temporary truck drivers business might not be.

When the Human Cloud sector has matured, each 'natural territory', defined by the strength of barriers, will likely be in the hands of one operator.

The natural monopoly territory phenomenon doesn't mean a small staffing business can count on grabbing a geographical and/or functional niche and holding onto it. The phenomenon means it's their only hope not their destiny. Also, any barriers may be short-lived in the sense that M&A will inevitably follow as larger players acquire businesses that captured natural territories to get control of it.

High shock sub-sectors will see the natural monopoly effect play out much faster than low shock. In either case, the natural monopoly feature of the Human Cloud will polarise the outcome between winners and losers with little mercy, and no one left in between, unlike the fragmented traditional staffing. Each territory will be a dog-eat-dog environment with one eventual survivor in the land grab.

Fork in the road

A staffing company must therefore choose to rise to the challenge or quit the game. In high shock sub-sectors, the choice should be made promptly but in less fast-disrupting niches there is no benefit in obfuscating. Inaction will eventually lead to a doomed Human Earth business.

In terms of valuations, in high shock niches, public and private valuations will crash unless the company is viewed as a successful converter and subsequent winner in Human Cloud. Valuations will polarise correlated with these winner-loser dynamics – whether a company is viewed as having a future on Human Earth or in the Human Cloud.

The choice is to get out of the old sector through a sale, or get in the new. To be more precise, staffing companies faces four logical choices: grow into the cloud fast organically if they have the ingredients; enter the cloud through acquisition where they don't or if barriers are too high; exit the sector through a sale before their valuation declines to the point where it is not worth doing a transaction; or watch their business decline organically without a transaction.

Disruption Database methodology

the1's Disruption Database works with the same approximately 80 staffing industry sub-sectors we use in our M&A work in the sector. They cover the most frequently-found niches based on common mixes of function, sector, and business model.

1. We take each sub-sector through the process of analysing the size of the existing market in terms of total staffing sector revenues associated with such niche and how that would have grown naturally from wage inflation and employment growth over five years as an imputed base before disruption impact.

2. The sub-sector is then analysed in terms of the disruption impact it will likely face from each of the six ingredients or drivers of disruption with a five-year time horizon.

3. We also consider the likely disruption in the sub-sector from both employers' and workers' points of view before arriving at the percentage of the sector revenues we expect will move to the Human Cloud.

4. The resulting value of disrupted revenues is what the traditional sector can be said to expect to lose and doesn't necessarily equate to the revenues of the Human Cloud sector because the new sector may charge clients differently and also because it will itself grow directly at the expense of end employers deciding to work through it where they would not have been working through the staffing sector before.

5. The percentage disrupted is called 'the1's Shock Factor'.

6. the1's 'Disruption Degree' is added to the sub-sector: EXTREME, SEVERE, STRONG, MEDIUM, MILD.

the1

the1 has completed more than 80 M&A transactions in the human capital sector in the US, UK and over 25 countries.

Buy-side

Methodologies

- Proactive search according to our 'Total Universe' approach
- Target Scoring & Prioritisation model
- Concurrent evaluation & negotiation methodology
- Joint Business Planning hosting
- 1-on-1 M&A techniques

USPs

- Expanding number, suitability and 'buy-in' of opportunities to:
  - avoid auction situations
  - deliver richer strategic fits
- Enhancing bargaining power through greater choice, and relative timing of discussions
- Resulting in the optimal transaction in the market based on highest synergistic IRR or client's own measure of value

Sell-side

Methodologies

- Proactive search according to our 'Total Universe' approach
- Acquirer Scoring & Prioritisation model
- Initial strategic fit review to optimise
- Concurrent evaluation & negotiation methodology
- Joint Business Planning hosting
- Well-timed auction dynamics post synergy discovery

USPs

- Review and recommendation on go-to market readiness to increase the client attractiveness
- Enhancing bargaining power by maximising number and strategic quality of bidders, and relative timing of discussions
- Resulting in the optimal transaction balancing value, deal structure, risk and other soft factors key to client.

Companies wishing further information on our services can contact info@the1.com.

the1

Blackwell House, Guildhall Yard
London, EC2V 5AE,
+44 207 556 1090

565 Broadway, 2nd floor
New York, NY 10012
+1 212 517 1850

the1.com

© 2019, the1

Optimal M&A timing

Some companies content themselves with doing 'a' transaction rather than 'the' transaction, which for emphasis we like to call 'the 1'. Even if a company finds a good transaction, it is rarely the optimal one.

The optimal transaction should be identified and captured. Sometimes the key driver is a particular strategic fit, sometimes it is the structure/valuation available but often timing can be the critical factor.

In the context of sector disruption, timing may indeed lead the decision, in which case the search for the optimal then becomes a question of finding the right deal and right partner available at that moment in time.

This paper on 'Disruption in Staffing' is focused on factors influencing the optimal moment in time.