

Enterprise Risk Management Services

Market Update

ERG PARTNERS

JUNE 2021 EDITION



Enterprise Risk Management Services Market Update

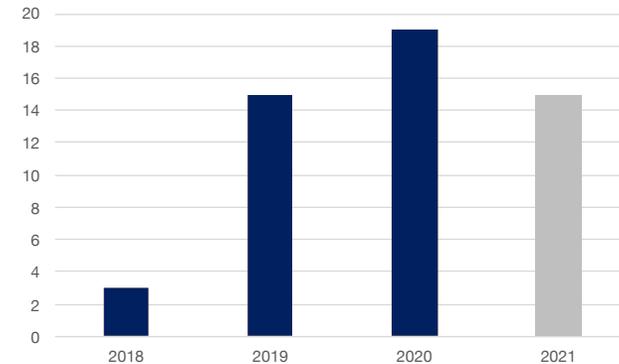
- The Enterprise Risk Management Services (ERMS) market, consisting of companies providing services ranging from investigations, business intelligence, background checking and pre-employment screening to security and cyber consulting, has largely recovered from the COVID related slowdown and returned to growth.
- Companies from the smallest specialists to the largest diversified companies are hiring globally to respond to increasing demand.
- Growth has been driven by capital market and transaction activity, including the growth of Special Purpose Acquisition Companies (SPACs). In order to take advantage of clients' evolving requirements, ERMS companies are pursuing new organic growth initiatives, such as ESG risk analysis.
- Companies also adapted their operating models by successfully transitioning to virtual delivery, rethinking their office setups and aggressively managing cost structures, which has made the industry even more profitable.
- Travel risk management and risk intelligence providers are well positioned to resume growth as corporate travel ramps up. However, security companies with high exposure to Afghanistan are faced with uncertainty following the withdrawal of US and other international forces.
- Against these positive industry trends, the ERMS market has experienced significant M&A activity. In this note, we provide an update on the sector M&A activity this year and offer our view of the outlook for 2022 and beyond.



M&A Activity in the ERMS Market

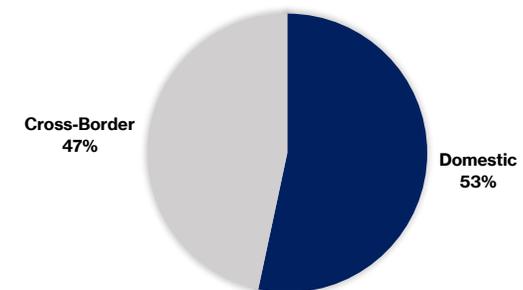
- M&A activity in the ERMS market continues accelerating and is significantly ahead of last year: In the first five months of 2021, 15 deals were completed, compared to 19 in the entire 2020.
- Most of the completed transactions in the first five months of the year involved small or medium sized targets. The principal exception was Allied Universal's acquisition of G4S following a bidding war with GardaWorld.
- Investors are interested in companies with services across the ERMS spectrum; transactions in 2021 included:
 - Security, training and capacity building
 - Strategic advisory, including political risk advisory
 - Cyber security
- Given the limited number of actionable targets, this does not provide the full picture of buyer/investor interest. Based extensive discussions with industry participants, we see significant demand for differentiated companies offering:
 - Recurring revenue (Subscription) models
 - Specialized open-source intel/investigations companies
 - Disinformation & online digital risk management
 - Financial investors are particularly interested in pursuing industry roll-up strategies to build market leaders with scale and ability to take market share from incumbents

No of Transactions 2018 – 2021*



* January – May 2021

Domestic vs. Cross-Border 2021**

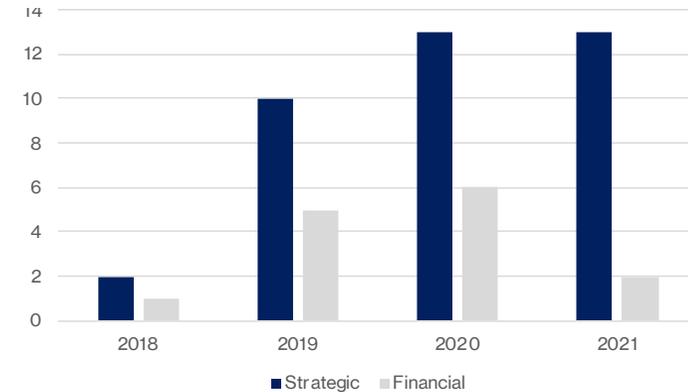


** January – May 2021

M&A Activity in the ERMS Market (Continued)

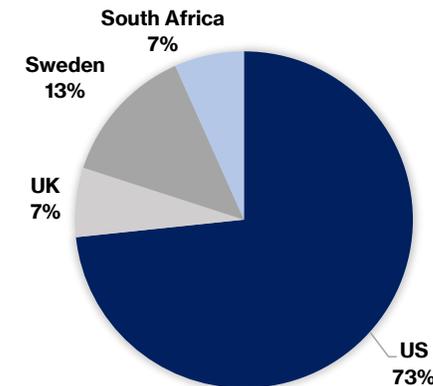
- Strategic buyers' role continued to dominate the ERMS M&A market accounting for eleven out of twelve deals.
- However, this understates the influence of financial investors: Some of the strategic buyers are backed by PE firms.
- Acquirers seek to create value by building scale, expanding into new markets, broadening the service offering, or diversifying the business model (higher margins, more scalable, technology enabled services or recurring revenues).
- The number of cross-border deals, which were depressed a result of COVID lockdown and travel restrictions, increased from 16% in 2020 to 47% of all transaction in the first five months of 2021., there were only 3 cross-border transactions in 2020.
- US buyers' dominance increased: 73% of all transactions involved US buyers. However, 53 % of all targets were UK based vs 47% US.
- Security companies pursuing deals to diversify their service offering were some of the most active buyers in the market.
- There were no serial acquirers: IDS International, a US security, training and cyber company, and Tempest, a Danish security provider, were the most active buyers in the first five months of 2021 with two completed deals, each.
- In nearly all transactions buyers acquired the entire share capital or a majority control. Two companies raised capital from investors: Ground Truth, an intelligence, and Immersive Labs, a cyber training company.

Strategic vs. Financial Buyers 2018 – 2021*



* January – May 2021

Acquirers by Country/Region Jan-May 2021



Valuations and Transaction Structures

The range of valuations in recent transactions has been expanding and depends on multiple factors:

- Buyers have been prepared to pay for certain strategically important targets, and large private equity backed companies have been able to take advantage of their low cost of capital. However, price sensitivity is undeniable and sellers with excessive expectations have not been successful.
- We have seen buyers increasingly focus on the sustainability and resilience of business - including recurring revenues and the leadership team's ability to manage costs.
- Buyers are focused on manage their risk exposure. As a result, most deals are highly structured. While we have seen transaction with no earnouts, equity rollovers are almost universally part of the deals to align incentives.
- Companies that lack differentiation,, diversified revenue sources and client base have generally not been successful in finding investors or buyers.

Key valuation drivers in recent transactions include:

- **Growth opportunities:** Buyers or investors will evaluate the mix of organic and inorganic growth drivers, focusing on the roadmap for future acquisitions.
- **Value of platform vs. individuals:** Buyers or investors focused on acquiring ongoing revenue generating platforms not dependent on few rainmakers. Targets that have built a broader and deeper client coverage model are significantly more attractive.
- **Uniqueness of skill sets and capabilities:** Hard-to-find skill sets and expertise, unique intellectual property, strong client relationships in a specific vertical, drive valuation multiples higher.
- **Repeat and recurring revenue:** Buyers tend to ascribe a higher value to revenues generated from subscription-based rather than project-based services. Even a high percentage of repeat business and long-standing relationships can result in higher valuations.
- **Revenue concentration:** From a risk-management perspective, buyers or investors get concerned if a large percentage of revenue is driven by a small number of large projects or from a few clients.
- **Management's track record.** In the current environment investors and buyers focus heavily on the managements track record of navigating through difficult times and, in particular, demonstrated ability to manage the cost in periods of negative revenue growth.

Deal Activity Summary

M&A Activity 2021 (January – May)

Buyer/Investor	Target	Target Business
Insight Partners etc	Immersive Labs	Cyber (Training)
Parsons	Blackhorse Solutions	Cyber
Group of investors	Ground Truth Intelligence	BI&I
Tempest	Fusion-85	IP investigations
Tempest	SCiSCO Global Solutions	BI&I
Gryphon Strategies	VLM Advisory	BI&I
Dentons	Albright Stonebridge Group	Strategic Advisory
Allied Universal	G4S	Security
Teneo	WestExec	Strategic Advisory
Kroll	RedScan	Cyber
First Advantage	GB Group	Background Screening
IDS International	Deco	Training, Capacity Building
IDS International	GSI	Training, Capacity Building
Paramount Group	Burnham Global	Training/Capacity Building
Flashpoint	CRFT	Cyber

M&A Outlook for 2021-22

Expected M&A Activity Driven by Strong Demand from Financial Investors and Strategic Buyers

- We expect interest and M&A activity in the ERMS market to remain robust in the second half of this year; a trend we believe will continue into 2022.
- Strategic buyers are pursuing acquisition strategies to diversify their service offering and revenue sources, access new client groups, shift their business model and to overcome the barrier to growth presented by the shortage.
- Various strategic buyers, often backed by private equity, are pursuing acquisition-led growth strategies to expand their global presence, broaden their service offering, access new client groups, and achieve scale to challenge the incumbent market leaders.
- The ability to travel and the global economic recovery will further facilitate deal-making.
- As the ERMS market continues recover and grow, we also expect more companies to try to take advantage of the strong market demand and seek a sale or a recapitalization in 2H2021 and 2022.
- Cross-border transactions are likely to continue to feature heavily, with US based acquirers in particular seeking to build a global presence.



M&A Outlook for 2021-22

Targets with Differentiated Offerings Will Attract Most Interest

- Most of the interest is likely to be focused on differentiated companies, which allow the buyer to better support clients' evolving requirements, including;
 - Specialists in emerging fields such as ERG risk, crypto asset compliance and blockchain analytics;
 - Experts in digital/open-source intelligence and investigations;
 - Strategic advisory, including political risk advisory; and
 - Fraud investigations and litigation support/dispute resolution companies, who will benefit from the post-crisis surge in demand for their services.
- We expect companies with proven recurring revenue/subscription models to be of particular interest to buyers and investors.
- In addition, we expect investors to look for investments providing technology solutions for fraud investigations, compliance issues and third-party risk assessment using data-sets, collection platforms and applications.

Valuations Are Attractive but Structured Deals Are the Norm

- We expect the valuation ranges in the sector to remain wide with buyers prepared pay high multiples for targets that fit buyers' strategic priorities
- Companies with subscription-based service models and a high level of recurring revenue are highly attractive to investors, and likely to attract the most attractive valuation multiples.
- However, buyers will continue to carefully manage their risk exposure, resulting in deal structures with relatively smaller upfront cash portions and larger contingent components.
- Private equity backed acquirers will continue to expect equity rollovers by management teams to ensure alignment of interests.

ERG Partners

Enterprise Risk Management Advisory Leadership

ERG Partners, founded in 2005, is an independent financial and strategic advisory firm with unrivalled Enterprise Risk Management Services sector expertise owned by its partners. ERG Partners offers the highest quality, independent advice to its clients across a broad range of corporate finance and strategic matters, including mergers & acquisitions, strategy development, scenario planning and restructurings.

Over the years, ERG Partners has worked with a full spectrum of ERMS companies including investigations, business intelligence, risk research, background screening, cyber and security companies helping them build and realize shareholder value.

ERG Partners combines in-depth industry expertise with market leading advisory skills, and prides itself on its excellent reputation, execution capability and experience in cross-border transactions.

Tapio Vaskio
Managing Director
Tel: +1 646 552 4038
Email: tvaskio@ergpartners.com

Arpad Krizsan
Managing Director
Tel: +1 646 250 8634
Email: akrizsan@ergpartners.com

Christian Tonsberg
Senior Adviser
Tel: +1 203 451 1374
Email: ctonsberg@ergpartners.com

Web: ergpartners.com

Disclaimer

© 2021 ERG Partners. All rights reserved. This material may not be reproduced in any format by any means or redistributed without the prior written consent of ERG Partners.

ERG Partners is a trade name for Enterprise Research Group LLC.

ERG Partners gathers its data from sources it considers reliable; however, it does not guarantee the accuracy or completeness of the information provided within this presentation. The material presented reflects information known to the authors at the time this presentation was written, and this information is subject to change. ERG Partners makes no representations or warranties, expressed or implied, regarding the accuracy of this material.

This presentation does not constitute advice or a recommendation, offer, or solicitation with respect to the securities of any company discussed herein, is not intended to provide information upon which to base an investment decision, and should not be construed as such. ERG Partners or its affiliates may from time to time provide investment banking or related services to companies mentioned in this presentation.