

# PROFESSIONAL EMPLOYER ORGANIZATIONS

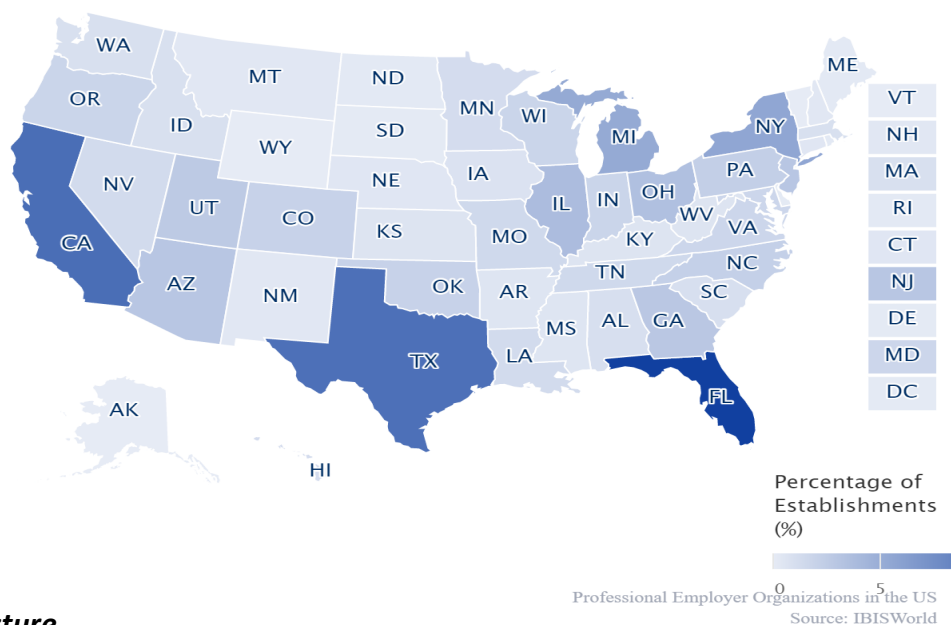
## 2021—2026 AT A GLANCE

### Government Regulations

Federal and state regulations surrounding professional employer organizations (PEOs) accelerated consolidation efforts, while generating additional barriers to market entry in 2021. As of August 2021, most states are enforcing requirements about licensing procedures and labor-related benefits.

State-level regulations are adding additional pressure to existing PEOs as litigation impedes forward progress toward expansion efforts. Regulation interpretations by several states is making it difficult for existing PEOs to enter new regions. Regulation variance has made it increasingly difficult for PEOs to enter new regions, and with impending federal regulation, that difficulty is expected to increase over the next five years. Industry-specific regulations will ensure proper workers' compensation, retirement and other benefits, and adequate reserves necessary for the future.

### Number of PEO Establishments\* in the US by State



### Geographical Structure

PEOs in states like Texas, Florida and California have less restrictive operating boundaries and can expand with ease to cover a larger geographical area. PEOs within smaller states will need to adhere to regulations from several states to gain the same operating boundaries. Hence, there are fewer PEOs in smaller states. While PEOs dominate the Southeastern, Southwestern, Rocky Mountains and Great Lakes regions, there are growth opportunities in more densely populated areas. Regional spread is dependent on several factors, though the increasing popularity of outsourcing is expected to boost PEO demand across a wider array of industries.

*\*An establishment is a single physical location where business is conducted or where services or industrial operations are performed. Term used synonymously with "offices." This PEO industry excludes establishments that provide business administration, recruitment and placement services, and establishments that provide temporary employees for short-term contracts.*

Source: IBISWorld

2021—2026 AT A GLANCE

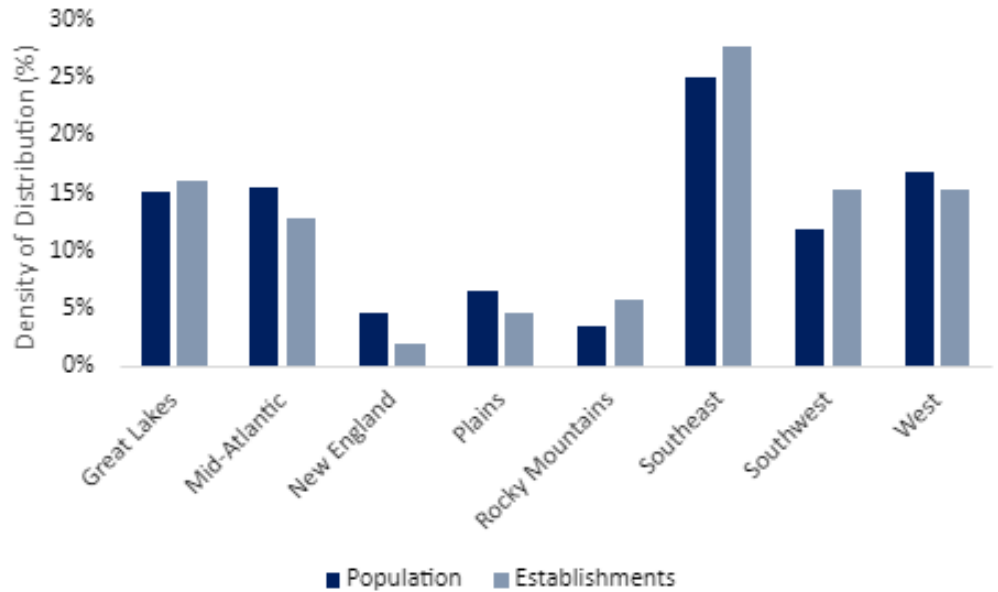
**Industry Standardization**

Federal regulations through the Small Business Efficiency Act (SBEA) created standardized regulatory frameworks in 2016, though most companies have not yet fully complied.

The number of companies in compliance is expected to gradually increase in tandem with the number of industry operators\*. However, profit expansion is projected to remain steady.

As a result of the pandemic, many companies shifted to a remote workforce, subsequently focusing on cost savings as revenues fell.

**Distribution of Establishments vs Population Density**



Source: IBISWorld

Operators absorbed compliance costs associated with government regulations, creating profit fluctuations within the industry. Despite increasing government regulation and work-from-home initiatives, market growth is expected into 2026 as financial reports show stabilized profits post-COVID.

**Competitor Constraints**

Robust M&A activity has expedited industry consolidation, while boosting individual market share opportunities. ADP Inc., Insperity Inc., and TriNet Group Inc. have the highest aggregate market share percentage of 6.2%, each operating with less than 2.5%. Consolidation of smaller PEOs by market leaders can generate greater returns before new PEOs enter the market.

However, as operators comply with regulations at an increasing pace and small and mid-sized businesses (SMBs) seek out PEOs for cost saving benefits, the barriers to entry should decrease relative to competition. Development of slightly differentiated services between similar PEOs will yield select or customized services rather than only offering options with the entire administrative process.

Revenue and new entrants in the U.S. PEO market are expected to steadily increase to almost \$248 billion and almost 4,200 establishments across the country. As COVID-19 volatility subsides, SMBs are anticipated to continue outsourcing administrative duties, more specifically payroll, to PEOs.

\*Industry operator is another term for PEO; PEO industry operators are responsible for the human resource management duties, employee administration and serve as the legal employer. They also pay wages or associated employment costs to employees on behalf of clients.

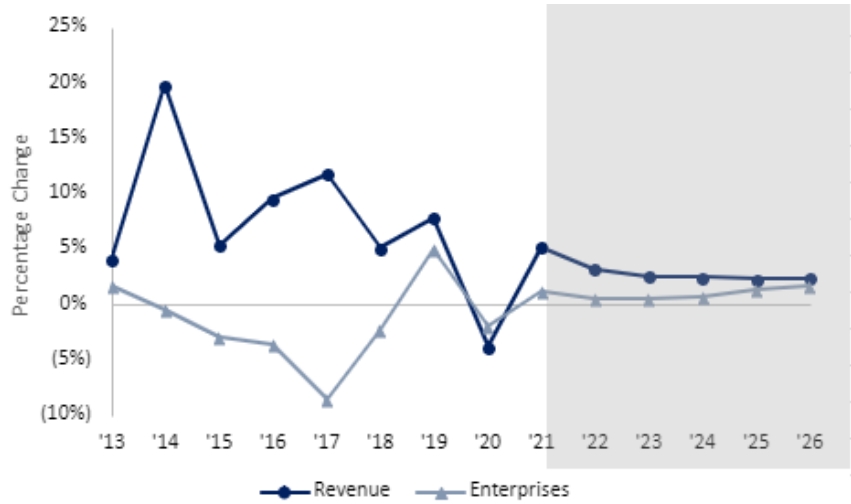
Source: IBISWorld Industry Report 56133

2021—2026 AT A GLANCE

**New Competition**

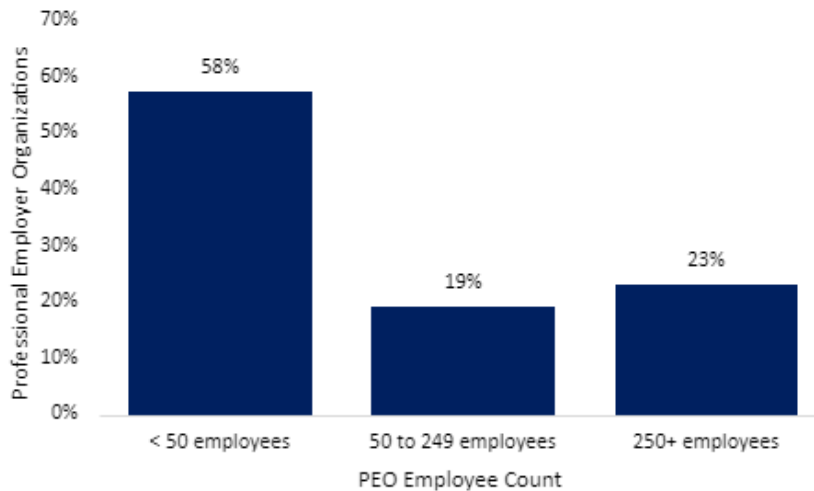
PEOs are expected to further penetrate the market by offering a broader range of benefits and services, most notably, comprehensive retirement plans and insurance coverage. These offerings should boost the attractiveness of outsourced HR and administrative resources to SMBs. However, SMB outsourcing is influenced by a low unemployment rate, among other factors. Assistance from Temporary Placement and Recruiting agencies can supplement vacancies and ultimately encourage SMB outsourcing.

**PEO Industry Performance 2013-2026**



Source: IBISWorld

**PEO Service Segmentation Based on Client Employee Numbers**



The appearance and prevalence of the “gig model” is a close economic competitor to PEOs as of late. The “gig model” or “gig economy” is a labor market characterized by freelance work or independent contract jobs that are typically short-term as opposed to a permanent job. Disruptive websites like Fiverr.com, Guru.com and UpWork.com offer temporary or contracted work opportunities through online coordination. The gig model may further limit market share opportunities from businesses that may have traditionally chosen a PEO.



Source: IBISWorld, Fiverr.com, Guru.com, UpWork.com

## PROFESSIONAL EMPLOYER ORGANIZATIONS

### 2021—2026 AT A GLANCE

#### CARLETON MCKENNA & CO:

*We believe businesses are the economic engine of our society, and that business owners deserve and require a proactive advocate to maximize life changing transactions.*



#### FIRM OVERVIEW:

Carleton McKenna & Co. is an independent investment banking firm providing M&A Advisory, Capital Raising, and Pre-Transition Advisory services. We deliver hands-on transaction execution, with clear, insightful strategy to drive extraordinary success.

We work with middle market closely-held businesses, multi-generational family businesses, portfolio companies of financial sponsor firms and divisions or subsidiaries of public companies focusing in Manufacturing & Specialty Chemicals, Consumer Products, SaaS, Healthcare, B2B Services and Cybersecurity.

Our Team is made up of finance and accounting experts, operators, C-Suite and Board professionals, lawyers, consultants, and marketing professionals. These diverse experiences and skills drive extraordinary results for our clients.

#### M&A ADVISORY TEAM:

##### Paul H. Carleton

Managing Partner  
phc@carletonmckenna.com

##### Christopher J. McKenna

Managing Partner  
cjm@carletonmckenna.com

##### Nora T. Mahoney

Principal  
ntm@carletonmckenna.com

##### Alexis M. Becker

Assistant Vice President  
amb@carletonmckenna.com

##### Andrew W. Lease

Analyst  
awl@carletonmckenna.com

##### Patrick T. Berry

Analyst  
ptb@carletonmckenna.com

#### CARLETON MCKENNA & CO. DEAL TEAM AND CONTACT INFORMATION



Paul H. Carleton

*Managing Partner*



Christopher J. McKenna

*Managing Partner*



Nora T. Mahoney

*Principal*



Alexis M. Becker

*Assistant Vice President*



Andrew W. Lease

*Analyst*



Patrick T. Berry

*Analyst*