

Catching Apple

This report explores the drivers behind the ongoing transformation of the creative services industry from a highly-fragmented collection of small service providers with limited offerings to large, vertically integrated service providers. As a result of this transformation, we believe that there has never been a better time to sell a creative services firm. The amounts that buyers are currently willing to pay for creative services firms are double (or more) the historical levels.

This ongoing transformation has been fueled largely by what we call the “Apple effect.” Companies across a variety of industries are attempting to replicate Apple’s fully integrated, industrial design led approach to strategizing, designing, manufacturing, selling and marketing products and services. Unlike Apple, most companies are looking outside their corporate walls to implement this strategy. Rather than transform their companies into the next Apple, companies are turning to external service providers for a quick fix. This report will focus on the impact of this trend on acquisitions.

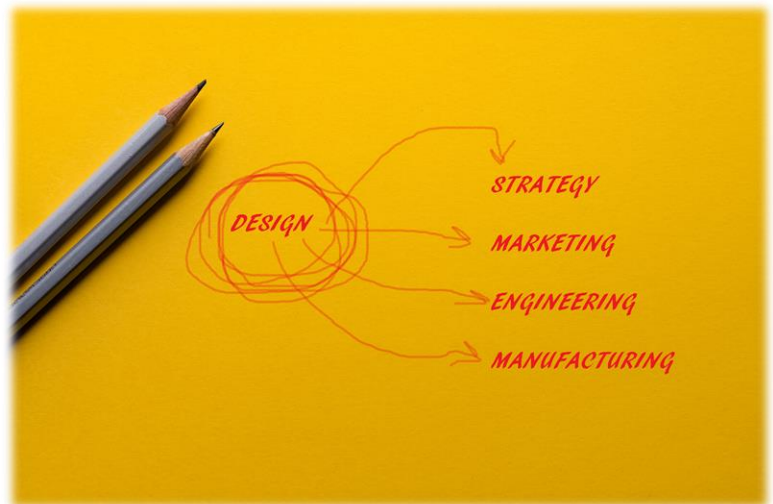


We define the creative services industry as a collection of companies that offer strategy, industrial and engineering design, user experience, advertising and manufacturing management services. Historically, companies relied on industrial design for the rather limited physical instantiation of products. Today, companies are recognizing the importance of design across their entire value chain. Companies (typically older and entrenched) that do not recognize this change are losing to newcomers that do. A great example of this is Nest’s thermostat and the challenge it poses to Honeywell and other traditional thermostat providers. This same story is playing out in a wide variety of other industries. New competition from design-focused upstarts such as Nest are forcing incumbents to incorporate a broad and coherent design philosophy. While the short-term trend is for companies to outsource this design transformation to external

service providers, we believe that, ultimately, the incumbents will be forced to transform their own organizations through both internal growth and acquisitions.

Apple was one of the first to implement an all-encompassing design philosophy. By taking full ownership of the development, manufacture and sale of its products and services, Apple created a dominant and highly profitable engine that is the envy of corporations around the world.

Our (very rough) world-view of this industry is shown to the right. It is this full suite of services that service providers are looking to offer. This somewhat-vertical (with design spanning the top to the bottom) integration of services offerings is the primary factor driving acquisitions in this space.



Unfortunately, the buckets used to categorize companies do not reach the level of granularity of the various services offerings shown above, and furthermore, individual companies often span many service offerings. We have grouped these services offerings into four categories so as to classify selling companies (targets). We fully recognize that this classification system is less than perfect.



Valuation

Although there is limited information regarding transaction values and multiples paid, our experience indicates that over the past year, the trend of large public companies purchasing small creative firms has pushed valuation multiples up into the 12X to 18X LTM EBITDA (twelve to eighteen times the most recent twelve months of earnings before interest, taxes, depreciation and amortization) range for “hot” properties. Traditionally, valuation multiples for creative services firms had been in the 5X to 7X EBITDA range, indicating an almost doubling of the value of any given creative services firm. While most creative services companies are being valued on EBITDA, some large sellers will have their revenues taken into consideration as well. We are seeing some creative services targets being valued around 1.3X – 2X LTM revenue, but the range is large, and the valuation received for any given company will depend on a variety of factors that we outline below. Given this increase in multiples, as well as the number of transactions consummated, it has never been a better time to be a seller in the creative services industry.



Not every creative services firm is created equal. While EBITDA multiples have expanded significantly in recent years, the premium paid for any given creative services firm is based on several fundamental factors. From a performance perspective, customer concentration and key performance indicators (KPIs) such as utilization come into play. If a majority of a firm's revenue is from one large client, the firm's business will be

deemed less attractive by most buyers, and receive a lower multiple and valuation. How effective a firm is in deploying its talent is also important, as buyers desire high utilization rates to ensure that assets are being deployed efficiently. Furthermore, a broad spectrum of services and offerings is also important, as buyers typically seek targets that can fill multiple service offering gaps. Additionally, scale and top line growth are also important. Large firms with high growth rates will fetch far higher premiums than those that are small and stagnant. Lastly, a competitive selling process can greatly increase the amount paid by a buyer. Retaining an advisor that can effectively market the strengths and, where needed, recast the weaknesses, of a firm can also substantially increase seller valuations.

Sellers AKA Targets

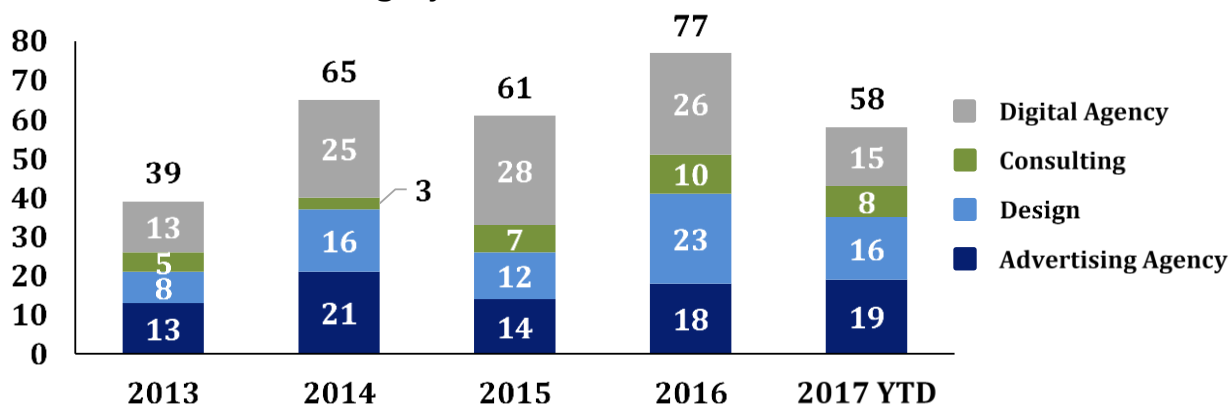
Design - Creating products and systems that optimize function, value, and appearance for the mutual benefit of the user and creator. Includes industrial / engineering / user experience (UX) design and manufacturing management.

Consulting - Providing thought leadership, unbiased partnership and deep industry knowledge to assist businesses with strategic decisions. Includes innovation, strategic and general consulting services as well as implementation.

Digital Agency - Create, plan and execute advertising / marketing strategies in the internet (digital) realm.

Advertising Agency - Create, plan, and execute advertising / marketing strategies in traditional and sometimes the internet (digital) realm.

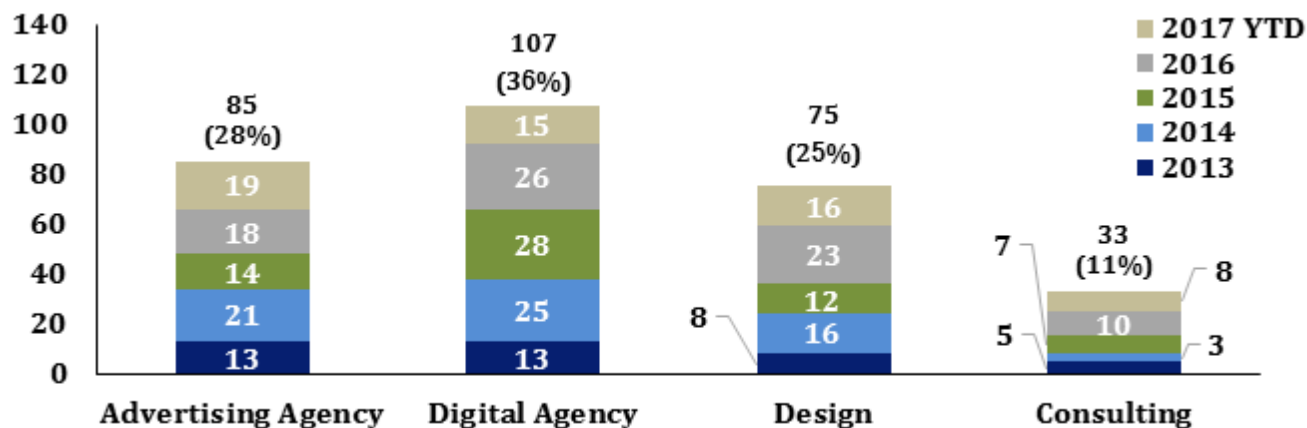
Since 2013, there has been a tremendous increase in M&A activity in the creative services space. In 2013, 39 transactions were completed, but in 2016, 77 transactions were consummated, representing a staggering 97% increase with most of sellers being digital agencies. Furthermore, 2017 is off to a hot start, with 58 deals completed through July 2017, which represents the YTD period in this report. If this pace continues, 2017 will be another record year in terms of deal activity in the creative services space. The below chart shows the number of transactions per year involving companies in each seller category.



Given the highly-fragmented nature of the industry, many creative services sellers are fairly small firms and as a result, public information regarding multiples paid is hard to come by. From our experience, most transactions are being priced as a multiple of the sellers most recent twelve months of earnings before interest, taxes, depreciation and

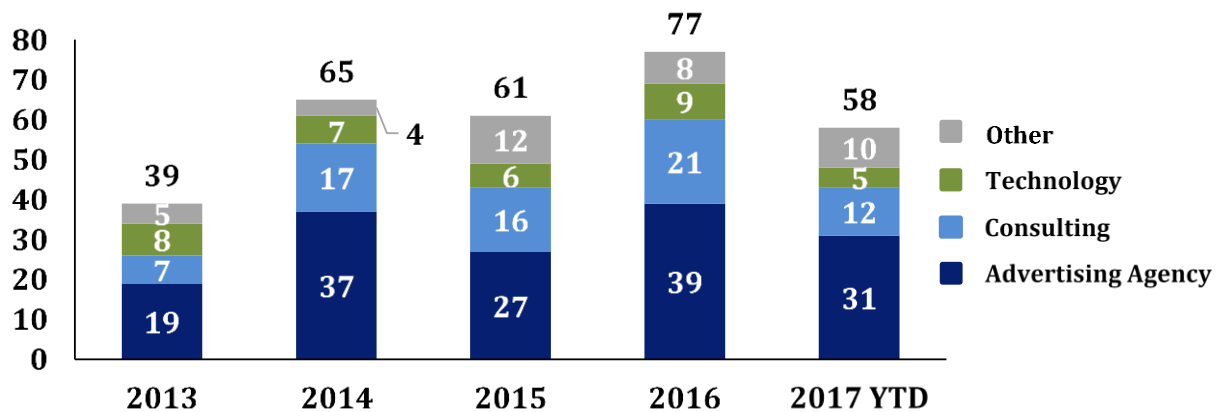
amortization (LTM EBITDA) and include two or three year earnouts. These earnouts typically represent 30% to 40% of the value paid by the buyers. Earnouts are a potential future source of conflict between buyers and sellers and are another reason many sellers employ advisors to help sell their firms. There is a very real chance for an earnout to lead to litigation (if not handled properly) but careful negotiation and proper drafting by experts in mergers and acquisitions should mitigate many of these issues. Likewise, an experienced advisor can help his or her client make normalizing adjustments to EBITDA so that the seller's financial performance is presented in an accurate manner to potential buyers.

Since 2013, digital agencies represented 36% of creative services industry transactions, followed by advertising agencies, accounting for 28% of acquisitions. Given the rise of digital content and social media, it follows that the appetite for digital agencies is expanding, as this medium has now become the most dominant force in communicating with consumers. Even across buyer groups, digital agencies were the most popular acquisition types. Design firms participated in only 75 transactions since 2013 and we expect this group to become more active in the future. With the growing importance of industrial design and user experience in product and service development, firms with related expertise should become more attractive. Thus, we predict there will be a noticeable increase in design M&A activity. The below chart shows the total number of transactions for each seller category from 2013-2017 YTD.



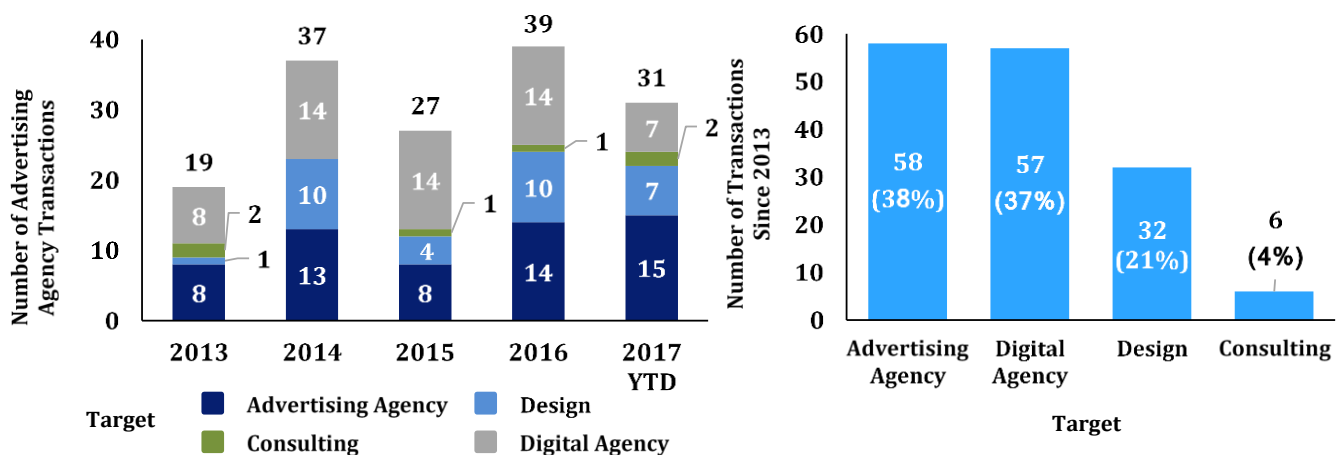
Buyers AKA Acquirers

The acquirers of creative services companies can be logically grouped into four categories: advertising agencies, consulting, technology, and other. The below chart shows the number of transactions per year completed by companies in each buyer category.



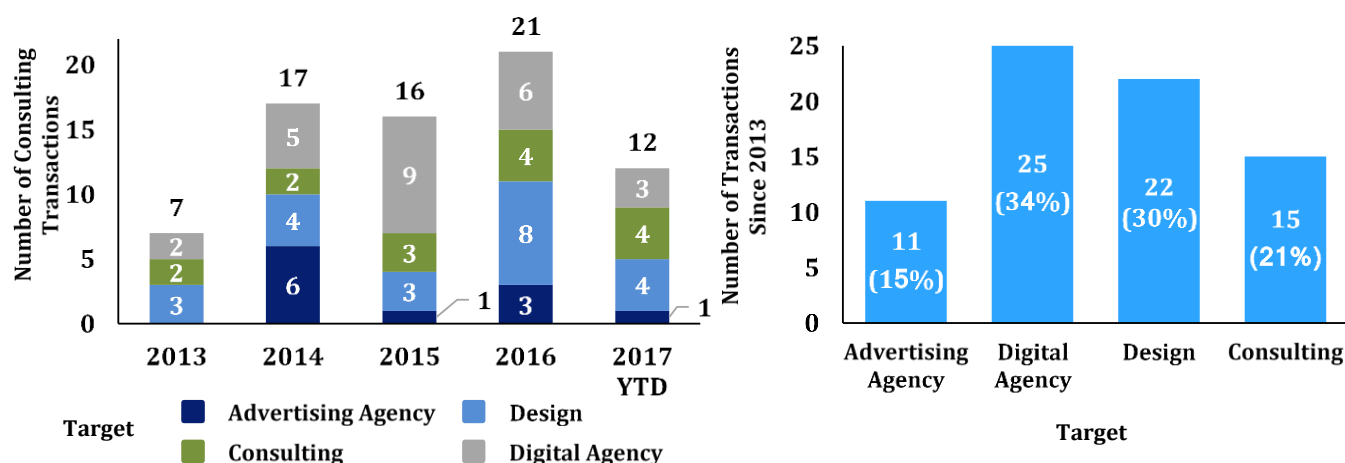
Advertising agencies have been the most active buyers since 2013, acquiring 153 creative services companies. Given the ongoing shift from traditional to digital media, it follows that traditional advertising agencies are acquiring digital agencies. Consulting firms were the second most acquisitive buyer group, purchasing 73 creative services targets as consulting firms look to broaden their service offerings to include industrial design and other services. We provide further insight into the strategic rationale for each buyer group later in this report.

Advertising Agency



Of all of the identified buyer groups, advertising agencies are the most active, acquiring 153 creative services companies since 2013. Some of the more active acquirers in this category include: Dentsu, Havas and BlueFocus. The focus of advertising agencies has been on acquiring digital advertising expertise and talent, as this medium has become the dominant format for today's marketer. Furthermore, ad agencies are facing tremendous competition from Google and Facebook, which collectively control almost 75% of the entire global ad tech market. In order to compete with these giants, agencies are drastically expanding their digital footprints and are on the hunt for leading digital shops around the globe to ensure their relevancy. Notable transactions by ad agencies include Publicis' \$114M acquisition of Nurun in September 2014, WPP's \$101M purchase of Syzygy in August 2015, and Dentsu's \$144M purchase of Smile Vun Group in April 2017.

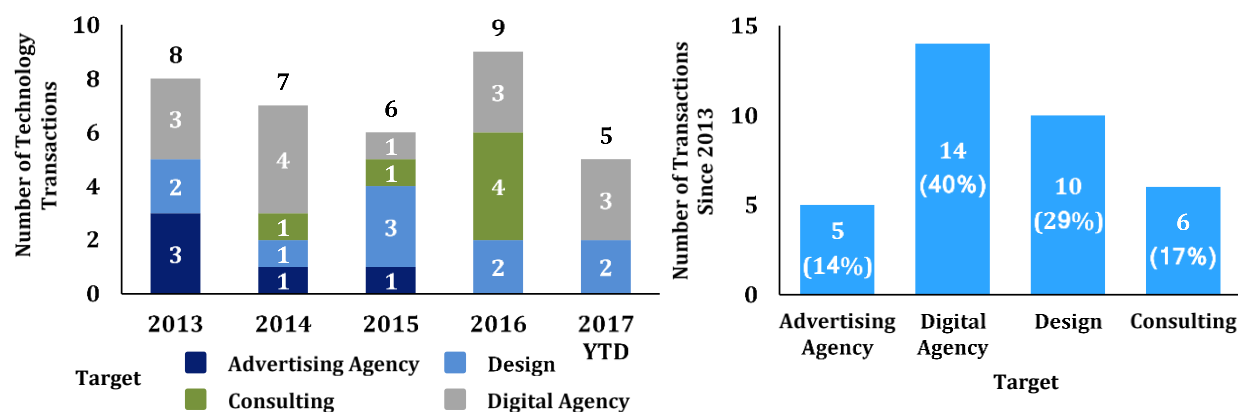
Consulting



Another active group of buyers has been consulting firms such as Accenture, Deloitte, IBM and EY. In today's dynamic world, consultants that provide only high-level strategic advice are finding that their clients want more. Clients are demanding to see at least some level of instantiation of products or services offerings recommended by their advisors. Demand for prototypes and social media engagement strategies is increasing, and in an effort to maintain relevancy, consultancies are swallowing leading digital agencies and design firms. These were two most active categories of acquisitions for consulting firms in the creative services space, accounting for 64% of their entire deal volume since 2013. For those firms focused on the implementation side of consulting such as Cognizant and EPAM, a need to move up the consulting food chain to higher margin services is an acquisition driver. This need to vertically integrate has pushed consultancies to become leaders in acquiring creative services properties, as evidenced by Wipro's \$103M purchase of Designit in July 2015, EY's purchase of Seren in August

2015, Cognizant's acquisition of Idea Couture in August 2016 and Accenture's acquisition of Altitude in January 2017.

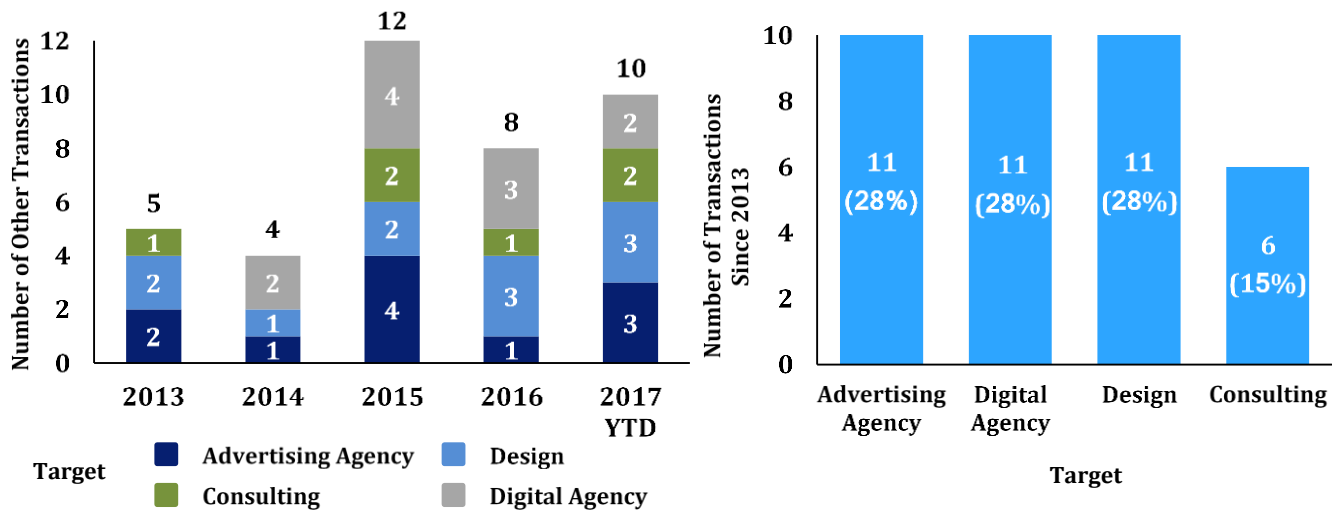
Technology



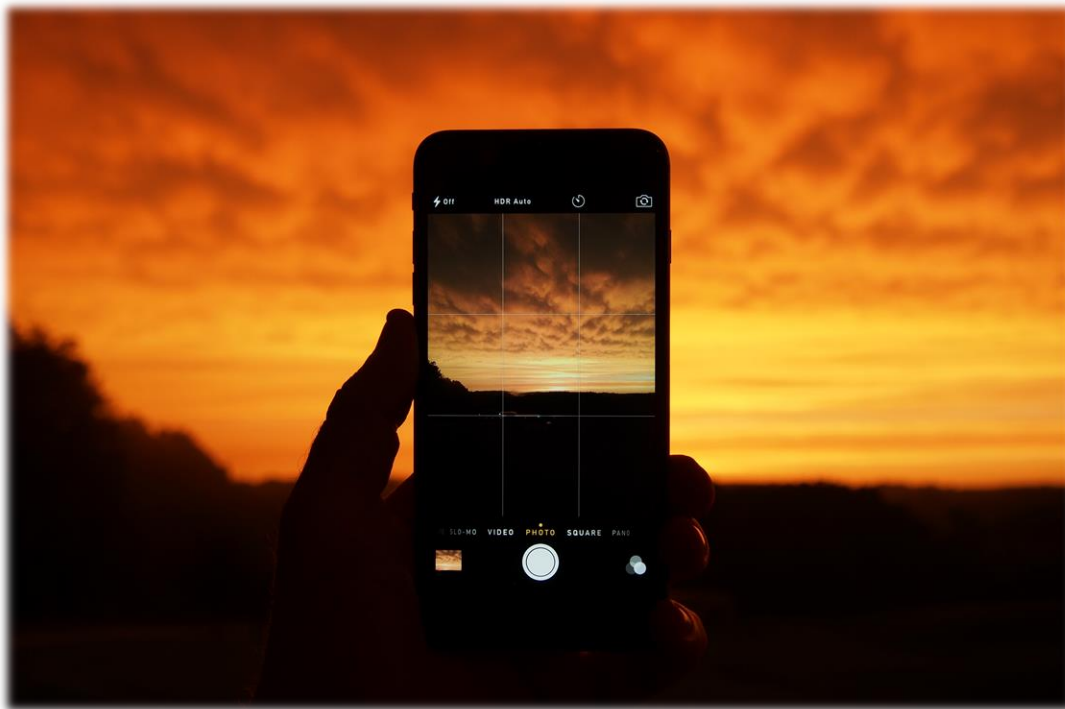
Leading technology companies have also demonstrated an active interest in acquiring creative services assets in recent years. Relevant examples of buyers in this category include Facebook, IDOX and Salesforce. The factors enabling these acquisitions are numerous, but the growing importance of design is a primary driver. A key example is Salesforce's acquisition of Gravity Tank, a leading innovation consultancy. By offering Gravity Tank's services to Salesforce customers and potential customers, Salesforce should be able to drive additional demand for its products and services. Technology companies also understand that design and user experience are now essential to creating a desirable product ecosystem, as evidenced by Facebook's Design team snapping up the partners at Teehan+Lax, a leading Toronto based design firm. By bringing design expertise in-house, technology companies can better defend competitive positions and ensure that designs remain proprietary.























Other



A multitude of companies from a broad range of industries have expressed interest in creative services companies over the past few years. For example, Capital One acquired two leading creative services firms, including Adaptive Path in October 2014 and Monsoon Company in July 2015. Given Capital One's recent foray into mobile wallets and financial technology apps for their consumer banking customers, Capital One stated that these creative services companies would help solve "experience design problems." Again, we see how design and user experience are becoming central to product development.



Notable Industry Transactions

Date	Buyer	Seller	Strategic Rationale
May 2017	 vivendi	 HAVAS	<ul style="list-style-type: none"> • “If this transaction is successful, it would enable Havas to leverage Vivendi’s skills in talent management, content creation and distribution. In return, Vivendi will gain access to Havas’s expertise in consumer science, data analytics and new creative formats.”
Feb 2017	 Capgemini <small>CONSULTING TECHNOLOGY OUTSOURCING</small>	 idean	<ul style="list-style-type: none"> • “Customer demand is shifting; service providers who bring digital design, creativity, and agility to redefine the customer experience are developing a strategic dialog with their clients, driving uniquely differentiated outcomes, and gaining market share as true digital partners”
Jan 2017	 sequence	 salesforce	<ul style="list-style-type: none"> • “Enhance Salesforce’s experience design capabilities, helping companies use the power of design to better connect with their customers in entirely new ways”
Jan 2017	 accenture	 ALTITUDE	<ul style="list-style-type: none"> • “Acquisition will result in a unique combination of Altitude’s innovation, design, and engineering expertise with Accenture’s industry knowledge and full range of consulting, technology and digital capabilities including artificial intelligence, cybersecurity and Internet-of-Things (IoT)”
Nov 2016	McKinsey&Company	 Veryday	<ul style="list-style-type: none"> • “Veryday is ahead of the curve because its work combines physical product design, service design, and an engaging experience. The convergence of physical and digital, of products and services, is a huge opportunity for a lot of our clients”
Jul 2016	 Cognizant	 idea couture	<ul style="list-style-type: none"> • Further advance Cognizant’s strategy to bring together elite capabilities in ideation, insight, strategy, design and technology to deliver innovative and impactful solutions
Aug 2015	 EY	Seren	<ul style="list-style-type: none"> • “The expectations of today’s consumers have been shaped by digitally native companies that offer simple and intuitive customer journeys for their products and services”
Jul 2015	 Capital One	 monsoon	<ul style="list-style-type: none"> • Capital One wants to “revolutionize banking with mobile apps but needs more workers than it could simply hire on its own”
Jul 2015	wipro digital	 Designit®	<ul style="list-style-type: none"> • Evolve Wipro’s digital offering • “Improve customer experience while radically digitizing business operations”
May 2015	McKinsey&Company	 LUNAR	<ul style="list-style-type: none"> • “Until now we couldn’t help clients with design execution. Bringing together top design, engineering, and business thinking in one holistic approach is going to be very powerful”
Oct 2014	 Capital One	 adaptive path	<ul style="list-style-type: none"> • “Solving experience design problems for Capital One”
Sep 2014	 PUBLICIS GROUPE	 nurun	<ul style="list-style-type: none"> • “Nurun’s expertise, based on a combination of design and new technologies, will strengthen Publicis Groupe’s digital global presence”

Viant Group

Viant Group is a boutique investment bank headquartered in San Francisco, California that advises creative services firms and other sellers. Viant Group manages each of its client's transactions from kickoff to close and brings its team's extensive transaction experience to bear on each engagement.

Select Creative Services Transactions

**idea
couture**

has been acquired by



*Acted as exclusive financial
advisor to idea couture*

fuseproject

has been acquired by



*Acted as exclusive financial
advisor to fuseproject*

Method

has been acquired by



*Acted as exclusive financial
advisor to and was a
principal investor in Method*

Cheskin

has been acquired by



*Acted as exclusive financial
advisor to Cheskin*

A comprehensive list of transactions that the Viant Group team has completed may be found at www.viantgroup.com. Viant Group's transactions are executed through its FINRA registered broker dealer, Viant Capital LLC.

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