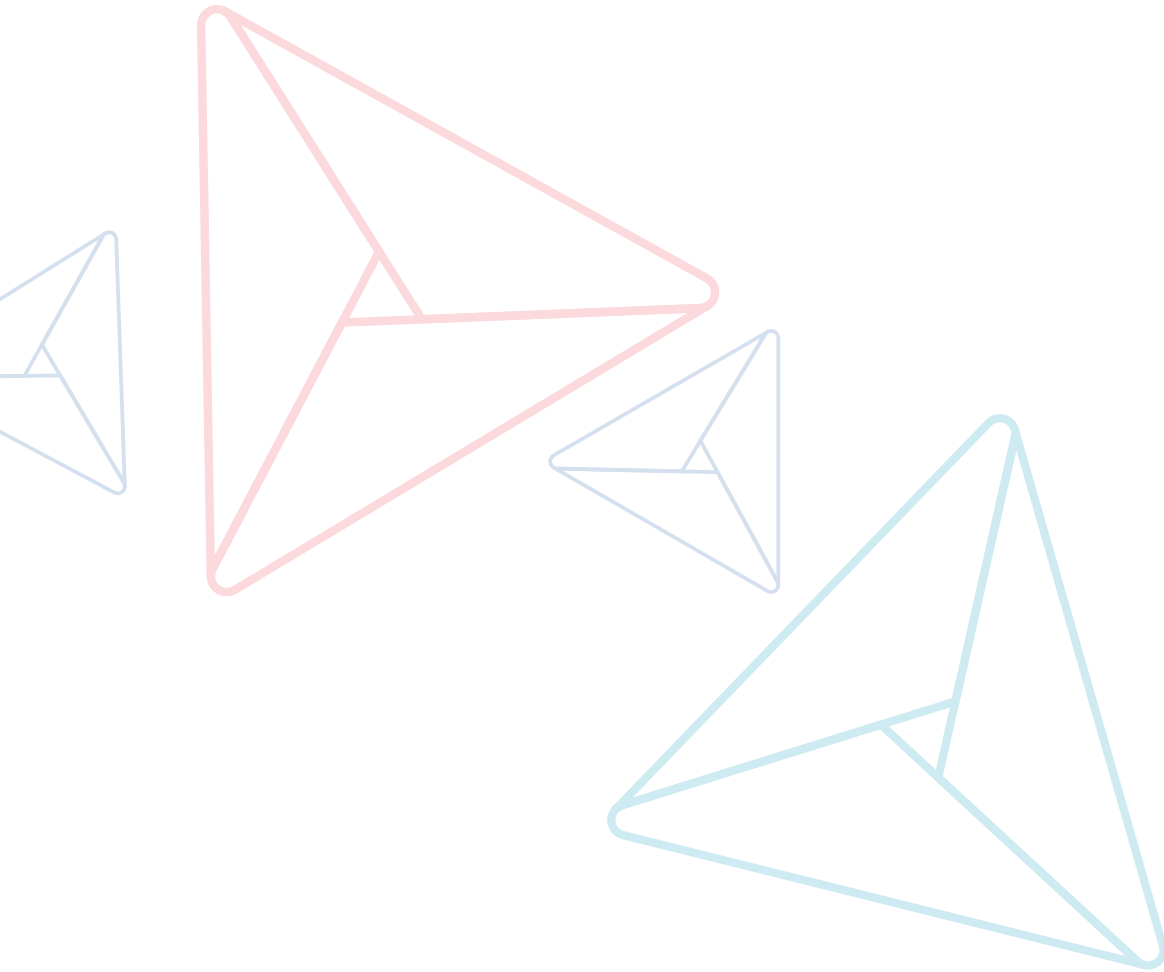




2020 HR SERVICE PROVIDER TRENDS REPORT

Industry Trends for PEOs, ASOs & Payroll Providers



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Introduction

Welcome to the fifth annual HR Service Provider Trends Report. In the spring of 2020, PrismHR surveyed professionals at PEOs, ASOs, and Payroll Providers about key business issues and trends.

The report also includes insights from two recent studies PrismHR conducted with small and medium-sized businesses (SMBs). Comparing the needs and views of SMBs with the HR service provider survey results reveals some interesting trends.

The report includes data from 131 HR service providers of all sizes. More than half (54%) of respondents are an executive/owner. A full profile of respondents can be found at the end of this report.

WHAT'S THE IMPACT OF COVID-19?

The COVID-19 pandemic of 2020 impacted SMBs and HR service providers alike.

Both worry about the short and long-term effects of the 2020 business shutdowns that blanketed the country from March to June 2020

The immediate need for SMBs to respond to government stimulus programs, lay off employees, and other disruptions led to increased workloads for everyone.

Some HR service providers expect to see significant reductions within their client base over the next 12 months, extending into 2021. Others believe it's too soon to tell what the actual implications will be for their business.

Read more about COVID-19 market effects in the following section.



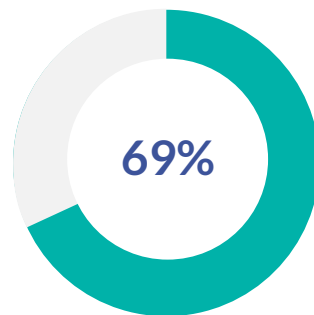
COVID-19 MARKET EFFECTS

Supporting Small Businesses Through CARES and FFCRA Legislation Changes

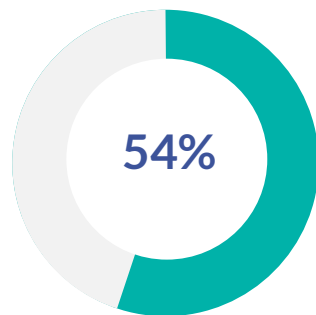
The COVID-19 pandemic and the accompanying business shutdown that stretched for several months (and is still affecting SMBs) resulted in a surge of client requests for HR service providers. Most found themselves providing clients with assistance navigating the Coronavirus Aid, Relief, and Economic Security (CARES) Act and the Families First Coronavirus Response Act (FFCRA).

While the initial tidal wave of urgent needs from SMBs has passed, the recession and aftereffects of the government stimulus measures will continue to provide challenges for the foreseeable future. The economic slowdown has forced many to cut costs, reduce staff, and look for efficiencies. As businesses reopen and prepare for a future in a changed world, service providers need to both respond to and anticipate the new needs of clients and worksite employees.

PROVIDED CLIENTS
CARES SUPPORT



PROVIDED CLIENTS
FFCRA SUPPORT

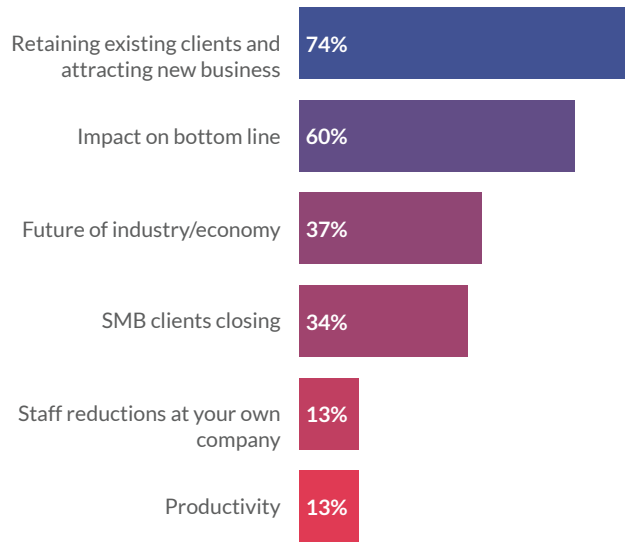


HR Service Providers Are Concerned About Their Clients' Revenue—and Their Own

Service providers anticipate many SMB clients will downsize and some may close permanently. They also recognize that outsourced services are often one of the first areas cut when businesses look for cost reductions. These trends are likely to negatively impact revenue retention and new business opportunities for many HR service providers.

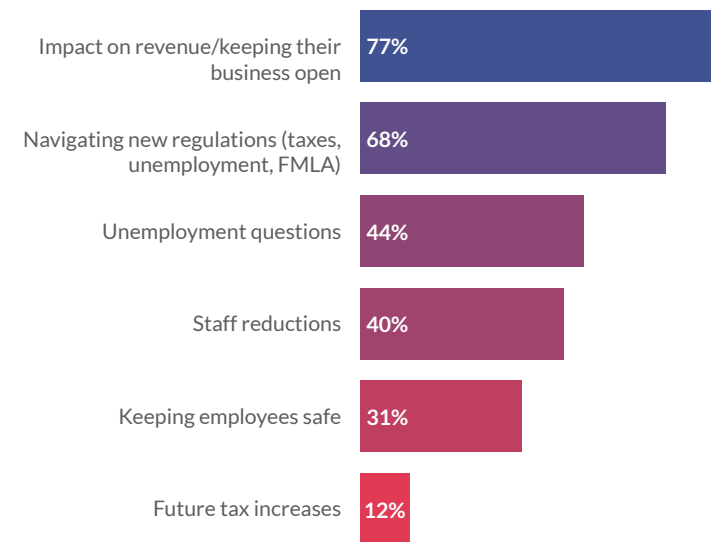
But as SMBs adapt to new normal, there is an opportunity to provide additional services (e.g., return to work programs, wellness) to support the changing needs of clients and their employees.

TOP HR SERVICE PROVIDER COVID-19 CONCERNS



TOP SMB COVID-19 CONCERNS

(according to service providers)

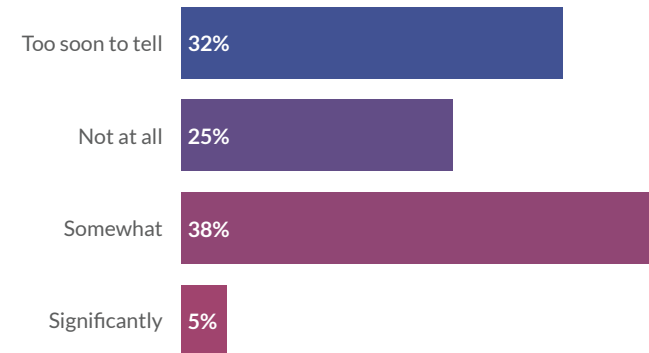


COVID-19 Impact on Client Retention

At the time of the survey, most HR service providers (57%) haven't noticed an impact on client retention or believe it's too soon to tell what the impacts will be.

That said, service providers recognize the challenges ahead. Customers closing their business has been the #1 reason for customer attrition throughout the five years of the Trends Survey. As business closings increase over the next twelve months, that driver will likely remain in the top spot.

COVID-19 IMPACT ON CLIENT RETENTION





SMB MARKET TRENDS

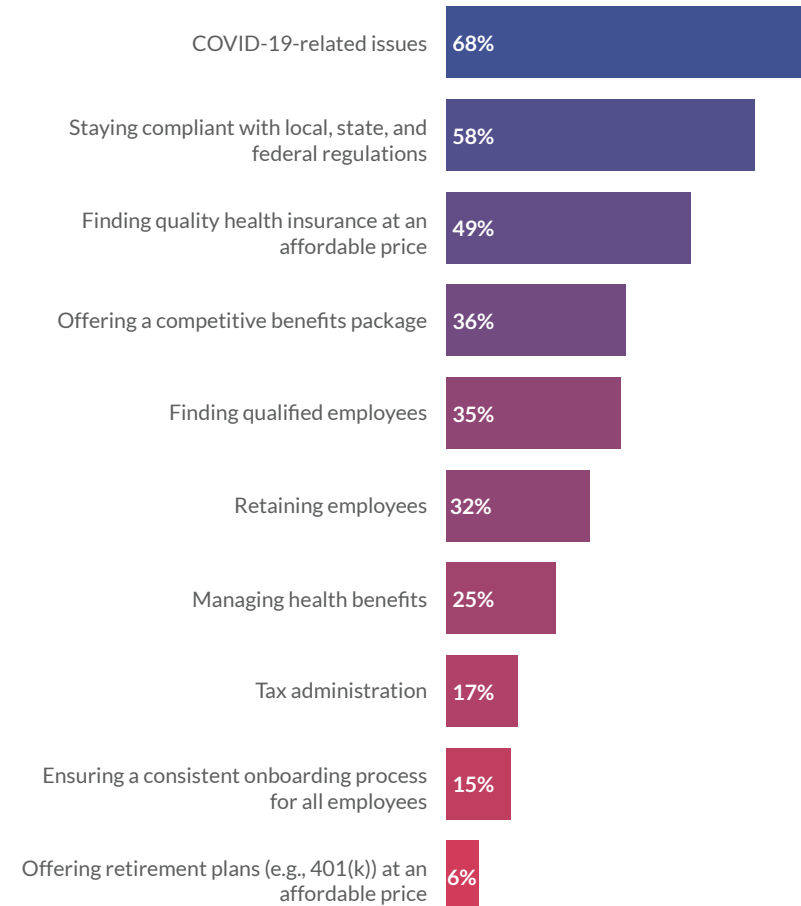
Top HR Challenges for SMBs

HR service providers anticipate that the biggest challenges SMBs will face for the foreseeable future relate to the COVID-19 pandemic and its aftermath: a recession, disruptions to normal operations, dealing with PPP and SBA loans, etc.

In a shift from last year's results, over half of service providers believe that SMBs will struggle to stay compliant with government regulations. The stimulus actions such as the PPP and a spike in layoffs and unemployment claims likely account for this change.

In a sliver of a silver lining, with unemployment rates so high and reduced competition for talent, HR service providers expect SMBs to find it easier to find and retain qualified employees than in previous years.

TOP HR CHALLENGES FOR SMB CLIENTS (REPORTED BY HR SERVICE PROVIDERS)

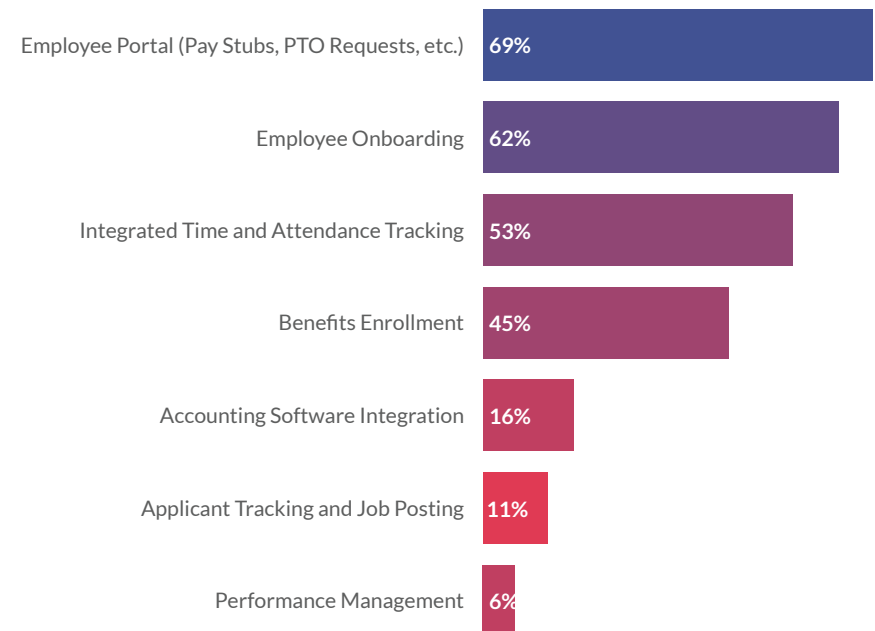


Top HR Technology & Solutions for SMBs

(ACCORDING TO HR SERVICE PROVIDERS)

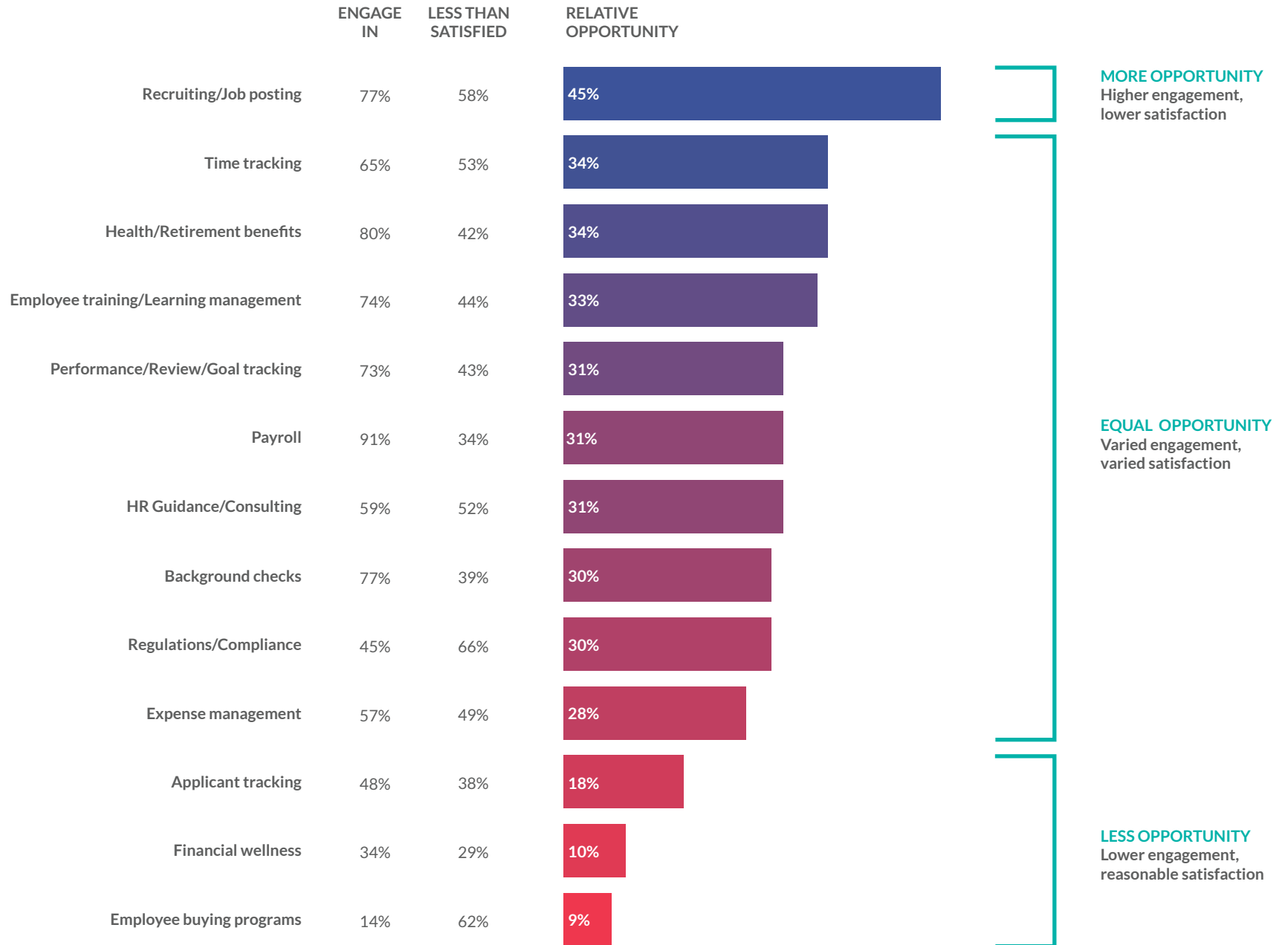
While it doesn't crack the top five in a list of most important HR technology for SMBs, applicant tracking and job posting is an opportunity service providers may want to take a closer look at. In a survey of SMBs, 77% engage in recruiting/job posting with more than half of those dissatisfied with their current process. And while the COVID-19 recession may reduce hiring, it will also likely increase the number of applications SMBs receive. This may make solutions that streamline the process even more appealing.

MOST IMPORTANT HR TECHNOLOGY FOR SMB CLIENTS



Most Important HR Technology & Solutions for SMBs

FREQUENCY OF HR ACTIVITIES & SATISFACTION WITH CURRENT CURRENT SOLUTIONS





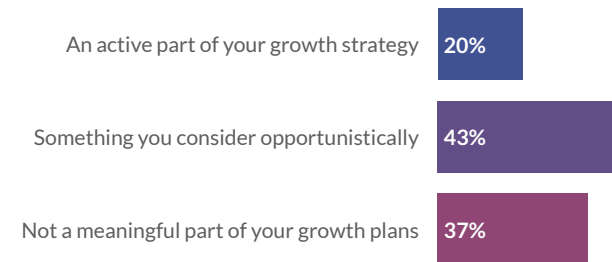
GROWTH TRENDS

Acquisition Strategies

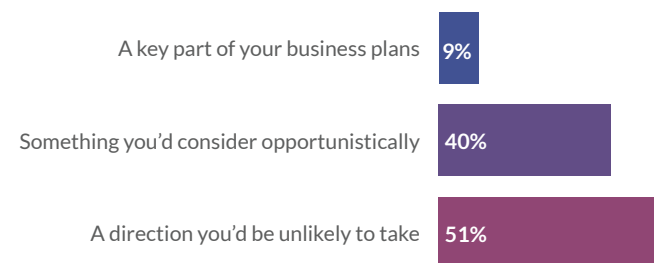
Owners split in terms of the role acquisition (either acquiring another firm or being acquired) plays in their long-term business plans. Acquiring other HR service providers would be considered by more than 60% of those surveyed, while about half would position themselves as an acquisition target.

HR service providers that report using acquisition for growth tend to be larger while no size differences exist in terms of those positioning their firm for acquisition.

ACQUIRING OTHER HR PROVIDERS



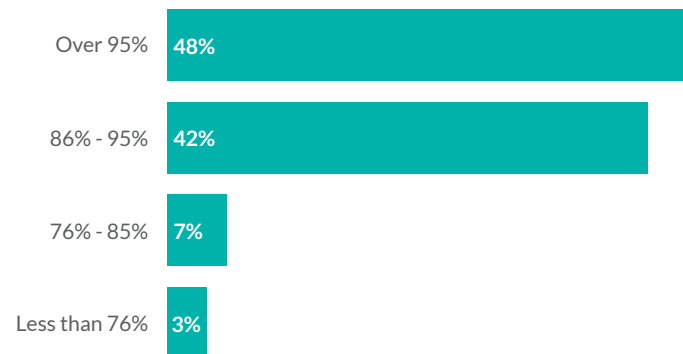
POSITIONING TO BE ACQUIRED



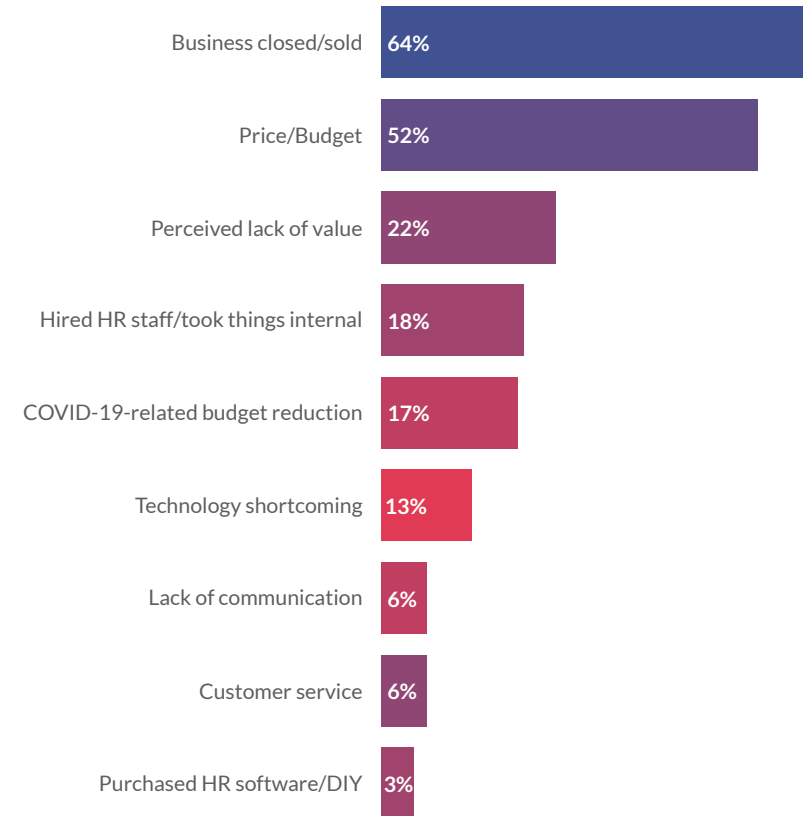
Retention

HR service providers have historically seen high customer retention. In 2020, nine out of ten service providers report retention rates of 86% or more. But given the impact of the COVID-19 pandemic on SMBs, we expect retention rates to decline in the year ahead due primarily to small businesses closing.

2019 CUSTOMER RETENTION RATE



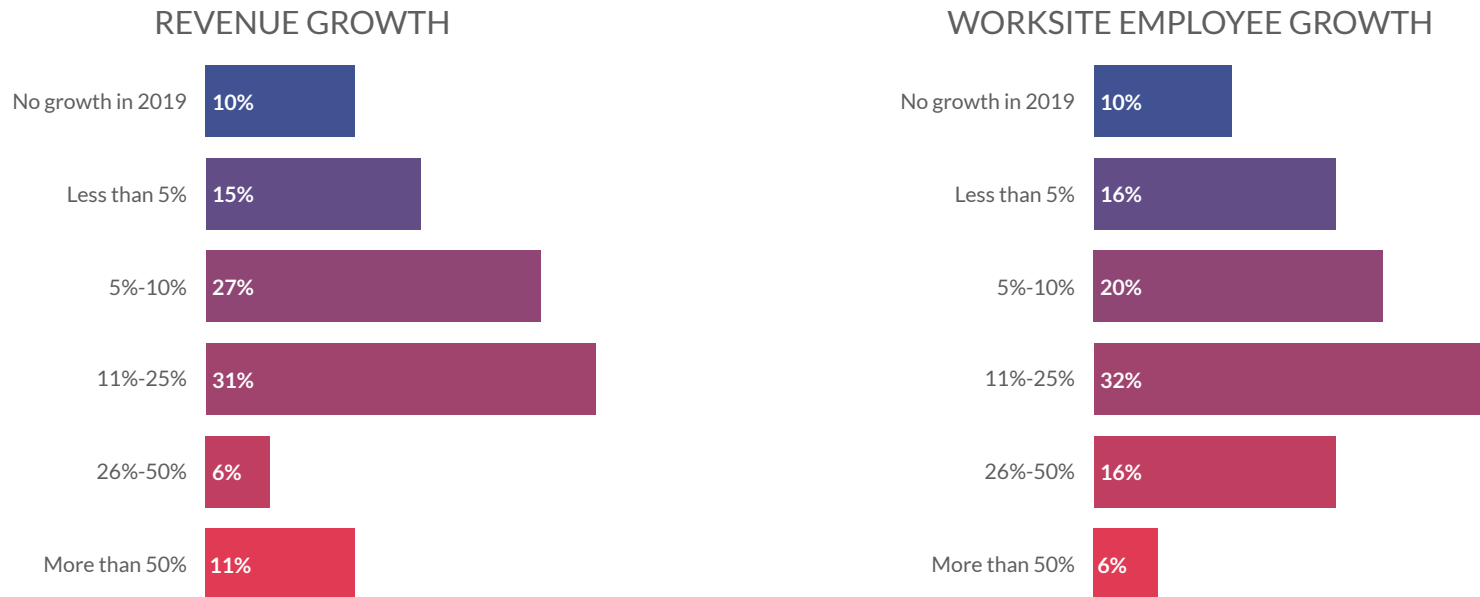
ATTRITION DRIVERS



HR Service Provider Average Growth

For most service providers, their 2019 worksite employee and revenue growth was consistent with growth rates from 2018 and 2017. The vast majority of respondents grew in 2019, with half of the market growing 5-25% in both WSE and revenue.

The 2020 Trends Survey did not ask respondents to predict their growth rate given the significant economic uncertainty. And while worksite employee numbers may be down for many of your clients, we're seeing many new SMBs sign on with HR service providers since the COVID-19 pandemic began. One could say the value an HR service provider can provide to an SMB has never been higher. In turn, recovering businesses are looking to partner with providers that can be a source of stability, efficiency, and guidance.





SALES & MARKETING

Provider Competitive Differentiation

Most HR service providers (84%) believe their competitive differentiation is the Level of Service they provide. Far fewer believe they differentiate on breadth of services, cost/time savings, or technology.

As you think about your business, how would your customers rank their needs on the list below?

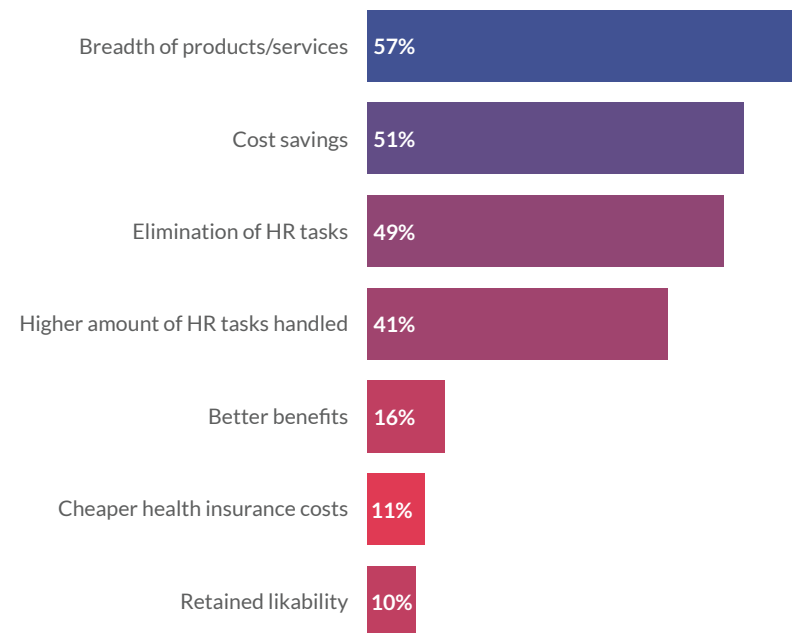
COMPETITIVE DIFFERENTIATION: RANKED

	TOP DIFFERENTIATORS (1ST OR 2ND)	1ST	2ND	3RD	4TH	5TH
Level of service	84%	64%	20%	10%	3%	3%
Breadth of services	42%	15%	27%	21%	14%	23%
Cost savings	31%	3%	28%	27%	32%	10%
Time savings	29%	16%	13%	22%	16%	33%
Technology, features, function	15%	3%	12%	20%	33%	32%

Reasons HR Service Providers Win New Clients

When asked to choose the top three reasons they win deals, service providers most often reported “breadth of products and services.”

Supporting a variety of client needs increases value and improves retention. And as the market changes due to COVID-19, expanding service offerings to address new and different client and worksite employee needs is becoming even more essential.



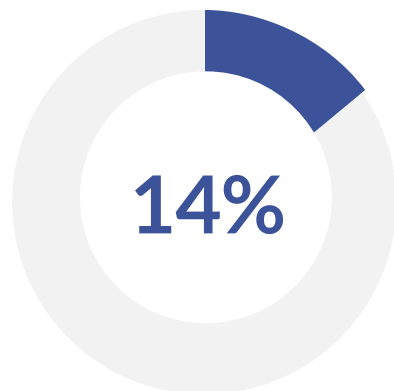
Reasons HR Service Providers Lose Deals

When service providers lose deals, the primary reasons reported are price or a prospect's existing relationship with a competitor. Lacking technology offered by a competitor is a factor in just 14% of cases.

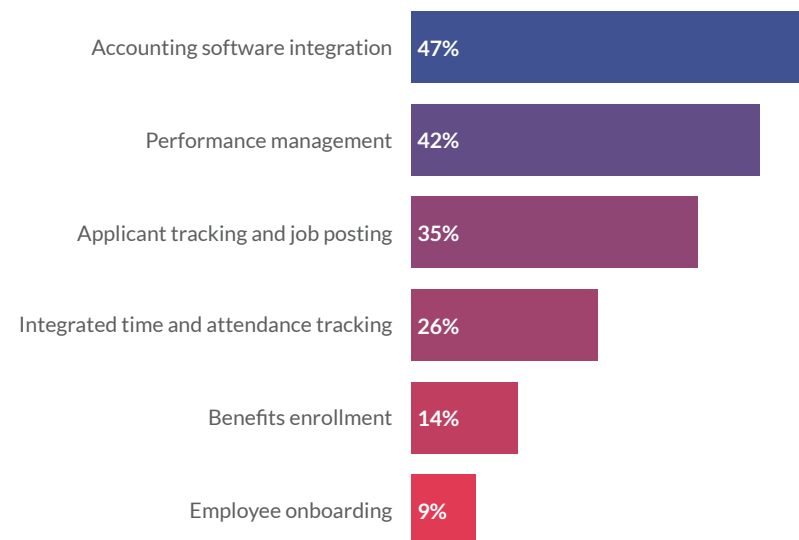
While technology isn't viewed as a major reason service providers lose deals, it's important to be aware of gaps in your offering. Near the top of the list are Performance Management and Applicant Tracking. We expect the adoption of these solutions to accelerate as businesses use technology to develop remote employees and keep them engaged while also managing an unprecedented volume of job applicants.

While a majority of HR service providers offer a relatively similar suite of services, it's important to remain connected with your technology provider to stay informed of the latest solutions, particularly during a time when SMB needs are changing.

LOSE DEALS DUE TO TECHNOLOGY GAPS



TECHNOLOGY OFFERED BY COMPETITORS THAT YOU LACK



Lead Generation and Marketing Effectiveness

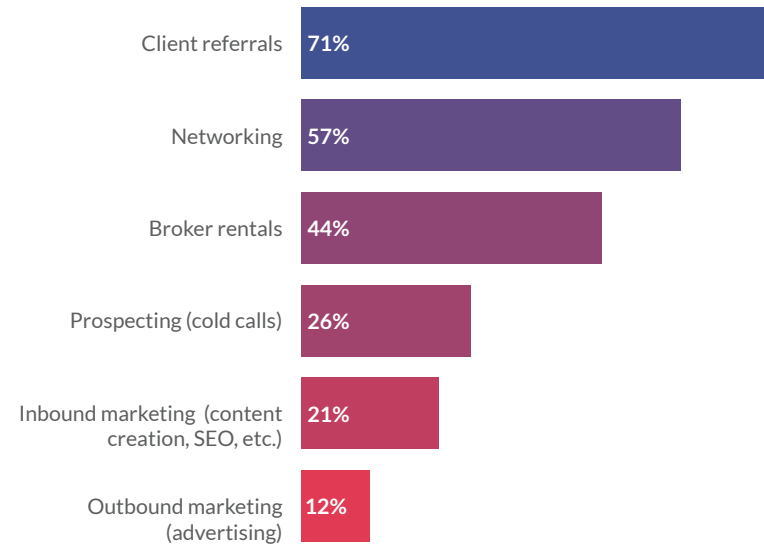
Referrals and traditional business development activities remain the primary sources of leads and top the list of most effective marketing activities. Inbound and other digital marketing activities continue to lag behind.

There are several factors that may contribute to these results:

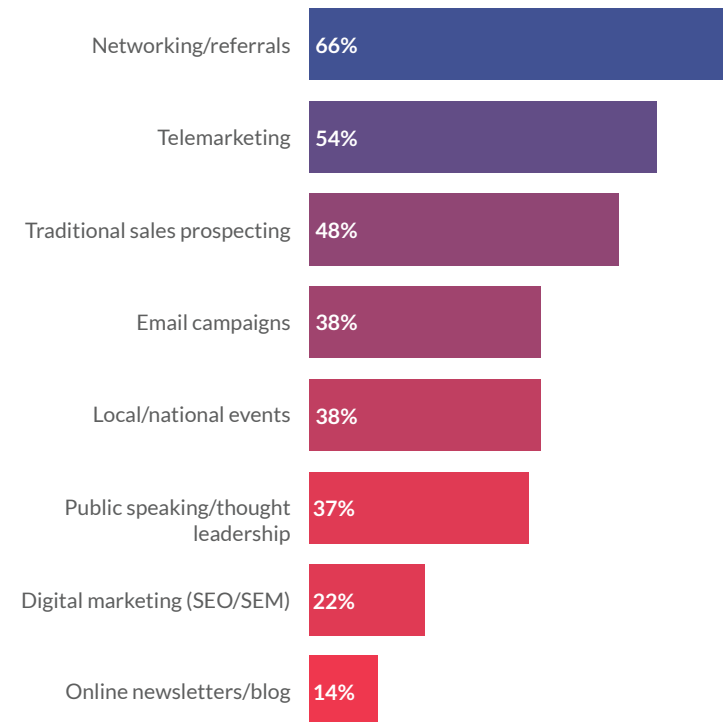
- Continued lack of awareness in the marketplace of the service provider value proposition
- Greater online search volume (and marketing budget) for point solutions and DIY software
- Service provider reliance on activities that have worked in the past and hesitancy to invest in building a comprehensive online marketing program

For all service providers, it remains important to take an educational approach in sales and marketing, particularly as the effects of COVID-19 drive new interest in this market.

SOURCE OF LEADS



MOST EFFECTIVE MARKETING ACTIVITIES





PROFILE OF SURVEY RESPONDENTS

Worksite Employees

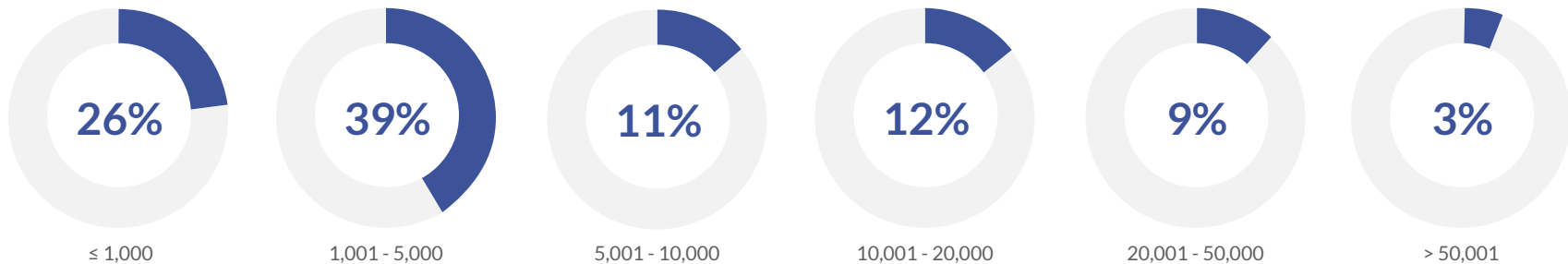
As in previous Trend Surveys, the majority of HR service providers (67%) support 5,000 or fewer worksite employees. The average and median number of worksite employees are 11,000 and 3,000, respectively. The average and median number of client organizations served are 330 and 150, respectively.

Half of service providers have fewer than 30 full-time staff, and two-thirds have less than 50 full-time staff. This makes them small businesses like the clients they serve.

This profile aligns with data from the National Association of Professional Employment Organizations (NAPEO) and reflects the makeup of the HR service provider market.

THE AVERAGE NUMBER OF EMPLOYEES SERVED IS
11,000

WORKSITE EMPLOYEES SERVED BY HR SERVICE PROVIDERS



Verticals Supported

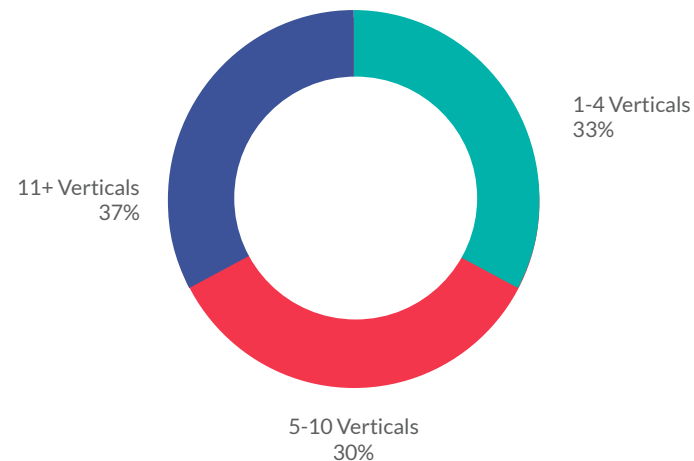
In a down economy, diversity in the verticals you support offers some protection when certain industries are impacted more significantly than others. While the impact of COVID-19 on businesses was widespread, industries that include hospitality, restaurants and entertainment were hit especially hard.

Most HR service providers serve a mix of industries rather than specializing in a specific type of business. Other research conducted by PrismHR indicates that the region of the country influences that mix. For example, those in the Midwest have more manufacturing clients compared to those on the West Coast which tend to have more technology clients.

THE AVERAGE NUMBER OF
VERTICALS SERVED IS

8

NUMBER OF VERTICAL SERVED





ABOUT THIS REPORT

The 2020 HR Service Provider Trends Report is the result of 175 responses from more than 131 different organizations collected through the annual PrismHR Trends Survey. Respondents come from a variety of roles within their HR service provider, ranging from payroll, benefits and HR to finance, IT and operations, as well as senior leadership, providing a diverse perspective on the HR outsourcing industry.

ABOUT PRISMHR

PrismHR creates industry-leading software and services that empower human resource service providers—including Professional Employer Organizations (PEOs), Administrative Service Organizations (ASOs), and Payroll Service Bureaus—to deliver world-class HR, benefits and payroll to small and medium sized businesses. PrismHR powers more than 88,000 organizations, delivering payroll, benefits and HR to more than 2 million worksite employees annually and processing greater than \$80 billion in payroll each year. For more information, visit www.prismhr.com.

