# Software M&A Recap

FIRST QUARTER 2023

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# Value scorecard driver: software ARR & services split

*EY Canada's Technology M&A team has developed a proprietary value scorecard tool to evaluate the relevant drivers that help drive a software business's value. In this quarter's thought leadership piece, we explore the contrast of annual recurring revenue (ARR) vs. services revenue for software businesses.*

## Value scorecard driver: software ARR vs. services revenue

Most software companies know that investors and buyers are drawn to recurring revenue streams. They also understand that support and services revenue is viewed as a less attractive counterpart and sometimes a distraction. However, almost all software as a service (SaaS) businesses have both. Consequently, a key value driver for software businesses is the split between software ARR and services revenue.

Let's dive into the evaluation of these revenue types and why we think these things must be viewed through the lens of the business as it stands today and where it will be at scale.

## What is software ARR and why do people want it to be a high percentage of total revenue?

Software ARR represents the predictable and ongoing revenue of a SaaS company, often taking the form of subscriptions, licenses or maintenance contracts. Simply put, software ARR is the recurring revenue generated by a company in a given month multiplied by 12. This makes it inherently a forward-looking number the quality of which relies on the highly sticky contracted nature of the revenue.

Software companies are often valued using a multiple of ARR, as it highlights important aspects of what makes a SaaS company attractive in the first place, such as revenue stability, customer retention and scalability. Given there is relatively low incremental cost to extend the service period of software or create a new instance, this type of revenue is often high margin.

It's worth putting a caveat here that the assigned value of ARR only materializes if it bears these characteristics (e.g., low churn, high margin, contracted revenues, scalability). In many cases a good litmus test to determine if revenue is truly recurring is whether it will be contracted in at least yearly increments and have features like autorenewal.

## What is service revenue?

While service revenue can be many things, broadly defined it is all the support and service required or sold alongside the software solution. In some cases, this revenue can be one-time in nature – such as implementation, consulting or setup – or it can be ongoing support or training on a contractually, recurring basis. It also can have a very different margin profile based on whether it is sold alongside the software subscription. Implementation can sometimes be quite low margin, while some value-added consulting – sold along with software – can be a meaningful profit driver and cash generator.

This broad definition makes it hard to look at service revenue as a simple statistic, but through the lens of the characteristics it shares with software ARR – scalable, high margin, recurring – the more favorably it will be valued. More important, there is a lot of nuance in understanding how services fit into the overall business model. While intensive implementations can slow down scale, they can also drive stickiness, because switching costs are high. They might also be associated with onboarding a more attractive enterprise customer. Ongoing support might require more organizational capacity to serve, but can provide a valuable feedback loop to the product and customer success team that helps drive organizational metrics.

Building a better working world

# Value scorecard driver: software ARR & services split continued

## Balancing ARR and service revenue

As a rule of thumb, an ideal situation is where services only make up 15%-20% of total revenues. But this should be evaluated in the context of the nature of the services and the value they bring to the business. In cases where services like support or training are considered contractually recurring components of the business, there is a possibility that service revenues can be higher without incremental impact on value.

If software ARR falls below a certain point, it may become clear that the business is in fact more of a tech-enabled service than a SaaS offering, which will change the valuation dynamics. Some considerations may be:

- Services may drive stickiness and upsell compared to the competition, particularly in industries where customers don't have the in-house resources to apply the full capability of the software, such as analytics, compliance or reporting solutions.
- At a certain level of scale, some or all of the services may be able to be offloaded to implementation or consultants, which could lead to a very different split at scale.
- Service revenues may be more significant, but may not actually require a large amount of resources and may be relatively scalable, which can make it a good way to generate cash flow, particularly in early stages.

## Key Takeaway: Look at the split, but also the narrative

The main takeaway for assessing how software ARR vs. services split impacts value is that, while generally software ARR is preferred and should be a significant majority, it is equally important to have a sound strategy on the interaction between ARR and service revenue types, as well as the ability for each of these revenue streams to drive the business model for the company, and a value proposition for end customers. Companies should think of this narrative based on where the split is today and where they believe it will be at scale.

Equally important to the software ARR vs. services split number is having the confidence in your chosen business model. When ultimately exiting your business, this narrative should form a clear part of your messaging and story.

## Ways to shift your business model toward recurring revenue

For companies looking to expand the percentage of recurring revenue over time, these are some of the ways it can be done:

- Prioritize product development to minimize service dependencies. Services can be decreased by addressing limitations such as customer onboarding, system integration, missing features and others.
- Embrace process automation to optimize workflow efficiency. A more self-service product will naturally require less support.
- Establish strategic partnerships for services as you scale. Establishing partnerships with third parties, such as consulting firms, will help scalability, so long as it is not at the expense of losing the relationship with your customers.
- Consider changing customer focus to a customer profile, which requires less services, support and customization to use the platform.

*Contact a member of our team if you're interested in learning more about our value scorecard along with other key parameters relevant to your business.*

# Some of our **recent deals include:**

**StepUp RGM**
has been sold to
**XTEL** RIGHT SOLUTIONS. SALES POWER.
backed by
**KANTAR** SilverTree
EY* acted as the exclusive financial advisor to StepUp RGM BV
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**Metrio**
has been acquired by
A technology company that operates leading stock exchanges and serves capital markets globally
EY* acted as the exclusive financial advisor to Metrio Software Inc.
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**VERDAZO**
has been acquired by
**Vela** SOFTWARE
EY* acted as the exclusive financial advisor to Verdazo Analytics Inc
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**3vGEOMATICS**
has been acquired by
**rst** INSTRUMENTS **MEASURAND**
RST/Measurand, a portfolio company of Vance Street Capital LLC
EY* acted as the exclusive financial advisor to 3v Geomatics Inc.
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**CORNERSTONE CAPABILITIES**
has been acquired by
An Industry Leader in Global Measurement and Data Analytics for Retail and Consumer Intelligence
EY* acted as exclusive financial advisor to Cornerstone Capabilities Inc.
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**refresh FINANCIAL**
has been acquired by
**Borrowell**
EY* acted as the exclusive financial advisor to Refresh Financial on its sale to Borrowell
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**WELLNESS CHECKPOINT®**
has been acquired by
**Carebook**
EY* advised InfoTech Inc., doing business as Wellness Checkpoint, on its sale to Carebook Technologies Inc.
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**filefacets**
has sold intellectual property rights and assets to
**DATA443** All Things Data Security (Stock Symbol: ATDS)
EY* acted as exclusive financial advisor to FileFacets, Inc.
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**FRESNEL SOFTWARE** **vitruvi**
received a strategic investment from
**AFL**
and
an Edmonton-based private investment company and family office
EY* acted as the exclusive financial advisor to Fresnel Software Corporation
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# Video Series

# Programmed for Success

EY's Technology M&A practice has recently launched a new video series, Programmed for Success

The 5-part series hosted by EY's Canadian Technology M&A Leader, Sid Nair interviews industry thought leaders from inside and outside of the firm. The series focuses on key considerations, risks and opportunities that should be considered prior to a sale of a technology business.

# Select
# Q1 2023 Transactions[1]

**Mar 20, 2023:** AAR Corp. (NYSE: AIR) acquired **Trax USA Corp.**, a leading independent provider of aircraft MRO and fleet management software to a diverse global customer base of airlines, MROs, and government aircraft operator, for a transaction value of $140.0 million.

**Mar 16, 2023*:** BioVaxys Technology Corp. (CSE: BIOV) acquired **TAETSoftware Corp.**, a Vancouver-based clinical studies management company engaged in the development and commercialization of the Trial Adverse Events Tracker ("TAET") technology platform, for an approximate transaction value of $1.4 million.

**Mar 14, 2023:** Blackstone Inc. (NYSE: BX) announced the acquisition of **Cvent Holding Corp.**, provider of a cloud-based enterprise event marketing, management, and hospitality platform for marketers, meeting, and event planners across the globe, for a transaction value of $4.6 billion. The transaction represents an enterprise value of 9.0x revenue and 34.5x EBITDA.

**Mar 13, 2023:** Symphony Technology Group announced the acquisition of **Momentive Global Inc.**, maker of SurveyMonkey, a software platform that enable customers to listen and act on stakeholder feedback, for a transaction value of $1.5 billion. The transaction represents an enterprise value of 3.2x revenue.

**Mar 13, 2023:** B. Riley Principal Investments, LLC announced the acquisition of **Synchronoss Technologies Inc.**, which develops software that helps streamline networks, simplify onboarding & engage subscribers to create new revenue and reduce costs, for a transaction value of $352.3 million. The transaction represents an enterprise value of 1.4x revenue and 8.4x EBITDA.

**Mar 12, 2023:** Silver Lake Management and Canada Pension Plan Investment Board announced the acquisition of **Qualtrics International Inc.**, provider of a cloud native software that helps organizations quickly identify and resolve points of friction across all digital and human touchpoints in their business, for a transaction value of $12.5 billion. The transaction represents an enterprise value of 8.2x revenue.

**Mar 06, 2023:** WW International, Inc., (NASDAQ: WW) announced the acquisition of **Weekend Health Inc.**, a subscription telehealth platform offering access to healthcare providers specializing in chronic weight management, for a transaction value of $132.0 million. The transaction represents an enterprise value of 4.2x revenue.

**Feb 17, 2023*:** Lumine Group Inc., (TSXV: LMN) acquired **Titanium Software Holdings Inc.**, which provides flexible and powerful platforms for telecommunication and government organizations to build out global carrier networks and secure private communication services, for an approximate transaction value of $56.0 million.

**Feb 16, 2023:** WiseTech Global (ASX: WTC) acquired **Blume Global, Inc.**, developer of a cloud-based digital platform that connects global supply chains into one ecosystem to drive asset optimization, predictive visibility, and traceability, for a transaction value of $414.0 million.

**Feb 14, 2022*:** The Descartes Systems Group Inc., (TSX: DSG) acquired **Windigo Logistics, Inc.**, doing business as GroundCloud, a cloud-based provider of final-mile carrier solutions and road safety compliance tools, for a transaction value of $218.0 million*.
**Includes earnouts of $80 million*

**Feb 10, 2023:** Parthenon Capital Partners acquired **Gaming Solutions Business of Global Payments Inc.**, and transition business into Pavilion Payments which will offer full suite of payments solutions for the gaming industry, for a transaction value of $415.0 million.

**Feb 09, 2023:** BitNile Metaverse Inc., (Nasdaq: BNMV) acquired **BitNile, Inc.**, operator of a technology platform that provides crypto mining, for a transaction value of $100.0 million.

**Feb 09, 2023:** Francisco Partners Management, L.P. announced the acquisition of **Sumo Logic, Inc.**, an operator of a SaaS analytics platform, which enables customers to deliver reliable and secure cloud-native applications, for a transaction value of $1.7 billion. The transaction represents an enterprise value of 5.0x revenue.

**Feb 02, 2023:** Leeds Equity Partners acquired **Talent Neuron**, a subscription-based provider of labor market data and analytics for corporate human resource and talent analytics teams, for a transaction value of $164.0 million.

**Jan 30, 2023:** Marqeta, Inc., (NASDAQ: MQ) acquired **Power Finance, Inc.**, develop of a cloud-native platform which offers credit card program management services for companies creating new credit card programs, for a transaction value of $275.0 million*.
**Includes earnouts of $52 millions*

**Jan 30, 2023:** WPF Holdings Inc., (OTCPK: WPFH) announced the acquisition of **Vezbi, Inc.**, developer of a user-driven Super App created that unifies and streamlines many features including tasks, events, messaging, micro-vlogs, snipbits, communities and intercom, among others into one centralised application, for an approximate transaction value of $4.8 billion.

**Jan 27, 2023*:** Metachain Holdings Inc., announced a reverse merger acquisition of Idle **Lifestyle Inc.**, which is specializes in the development and application of artificial intelligence technology, for a transaction value of $11.5 million.

**Jan 27, 2023*:** OpenWeb Technologies Inc., acquired **PowerInbox Inc.**, operator of a proprietary audience management platform which provides personalized, automated, and multichannel messaging solutions allowing publishers to drive new revenue with personalized audience engagement, for a transaction value of $100 million.

(1) Data sources: S&P Capital IQ, Mergermarket, Press Releases
**Deals indicated are Canadian deals*
All currencies are in US$

# Select
# Q1 2023 Transactions[1]

**Jan 24, 2023:** WiseTech Global Limited (ASX: WTC) acquired **Envase, Inc.**, a leading provider of transport management system software for intermodal trucking and landside logistics in North America, for a transaction value of $230.0 million.

**Jan 23, 2023*:** VitalHub Corp. (TSX: VHI) acquired **Coyote Software Corporation**, provider of software solutions to health and social service organizations, for an approximate transaction value of $1.8 million. The transaction represents an enterprise value of 1.5x revenue.

**Jan 23, 2023*:** Tiny Capital acquired **WeCommerce Holdings**, provider of a suite of ecommerce software tools to merchants to start and grow their online stores, for an approximate transaction value of $215.0 million.

**Jan 20, 2023*:** Thoma Bravo announced the acquisition of **Magnet Forensics Inc.**, a developer of digital investigation software that acquires, analyzes, reports on, and manages evidence from digital sources, including computers, mobile devices, IoT devices and cloud services, for a transaction value of $1.3 billion. The transaction represents an enterprise value of 13.2x revenue and 164.5x EBITDA.

**Jan 13, 2023*:** Imdex Limited (ASX: IMD) announced the acquisition of 40% stake in **Krux Analytics, Inc.**, which develops a drilling analytics software, focussing on the collection and analysis of exploration and production drilling data in real time, for a transaction value of $5 million.

**Jan 12, 2023:** Lessen acquired **SMS Assist LLC**, developer and operator of a cloud-based residential and commercial property management and facilities management platform, for a transaction value of $950 million.

**Jan 11, 2023*:** Cambridge Cognition Holdings Plc (AIM: COG) acquired **Winterlight Labs Inc.**, developer of a platform monitoring cognitive impairment through free-speech analysis, for an approximate transaction value of $8.5 million.

**Jan 09, 2023*:** Nuvei Corporation (TSX: NVEI) acquired **Paya Holdings Inc.**, a provider of integrated payments platform serving customers in growing end markets such as B2B, government, utilities, non-profit and healthcare, for an approximate transaction value of $1.4 billion. The Transaction represents an enterprise value of 5.1x revenue and 25.1x EBITDA.

**Jan 09, 2023:** Vista Equity Partners announced the acquisition of **Duck Creek Technologies Inc.**, operator of a platform which enables the property and casualty and general insurance industry capitalize on the power of the cloud to run agile, intelligent, and evergreen operations, for an approximate transaction value of $2.5 billion. The Transaction represents an enterprise value of 7.4x revenue and 392.2x EBITDA.

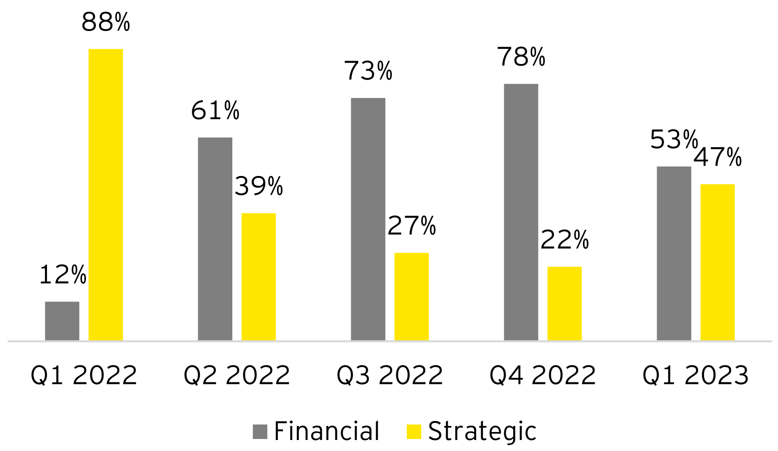
**Jan 06, 2023*:** The Descartes Systems Group Inc., (TSX: DSG) acquired Supply Vision LLC, which develops cloud-based shipment management solutions for North American logistics service providers, for a transaction value of $15 million*.
**Includes earnouts of $3 million*

**Jan 03, 2023*:** The Co-operators Group Limited acquired **Smart Employee Benefits Inc.**, provider of leading-edge IT and benefits processing software, solutions and services for the Life and Group benefits marketplace and government, for a transaction value of $58.7 million. The transaction represents an enterprise value of 1.5x revenue.

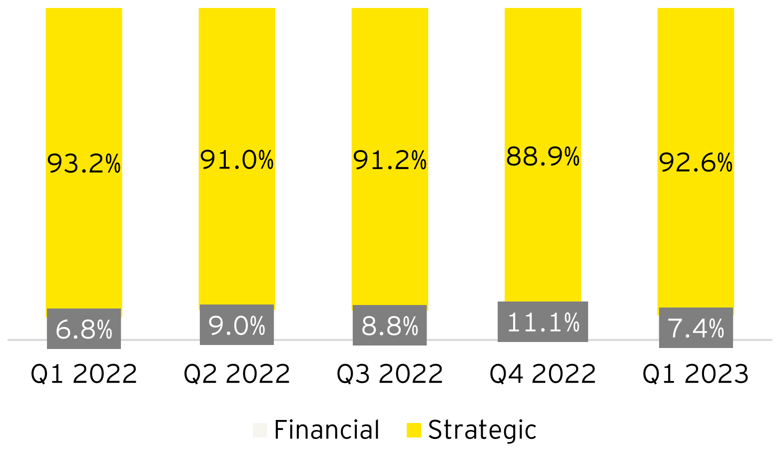
(1) Data sources: S&P Capital IQ, Mergermarket, Press Releases
**Deals indicated are Canadian deals*
All currencies are in US$

# Historical M&A **activity**

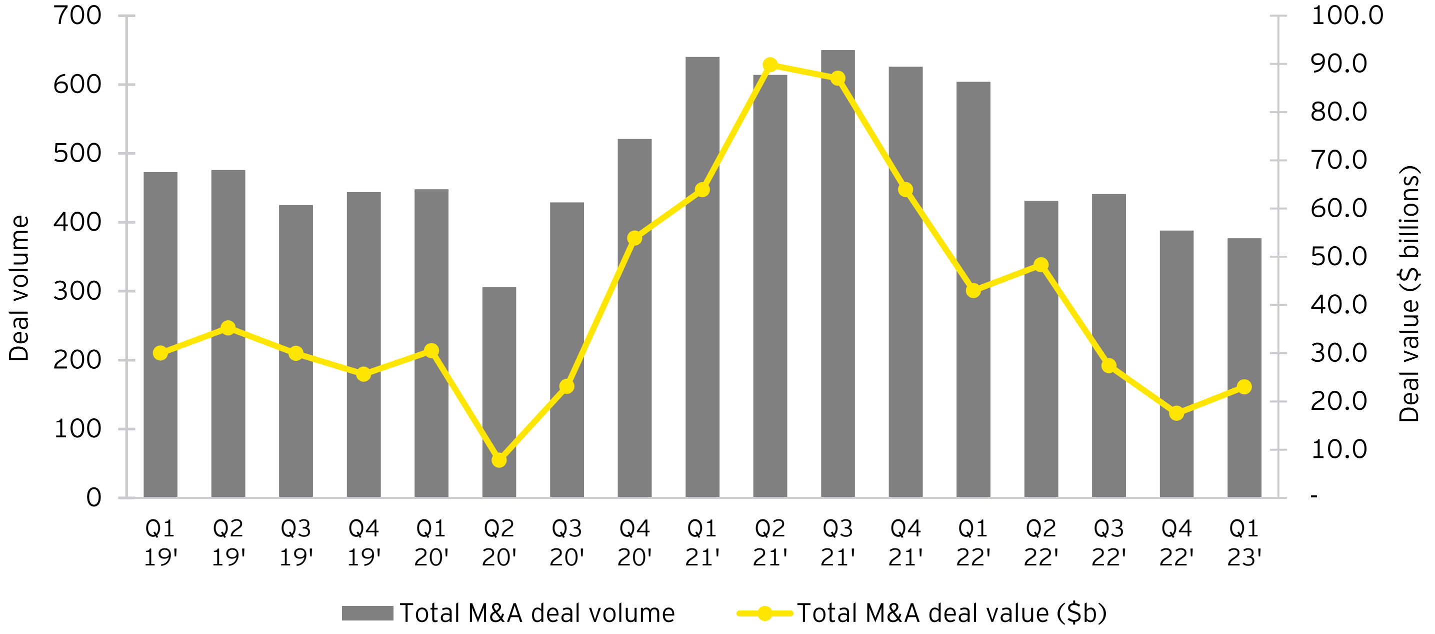
## Deal value by type of acquirer



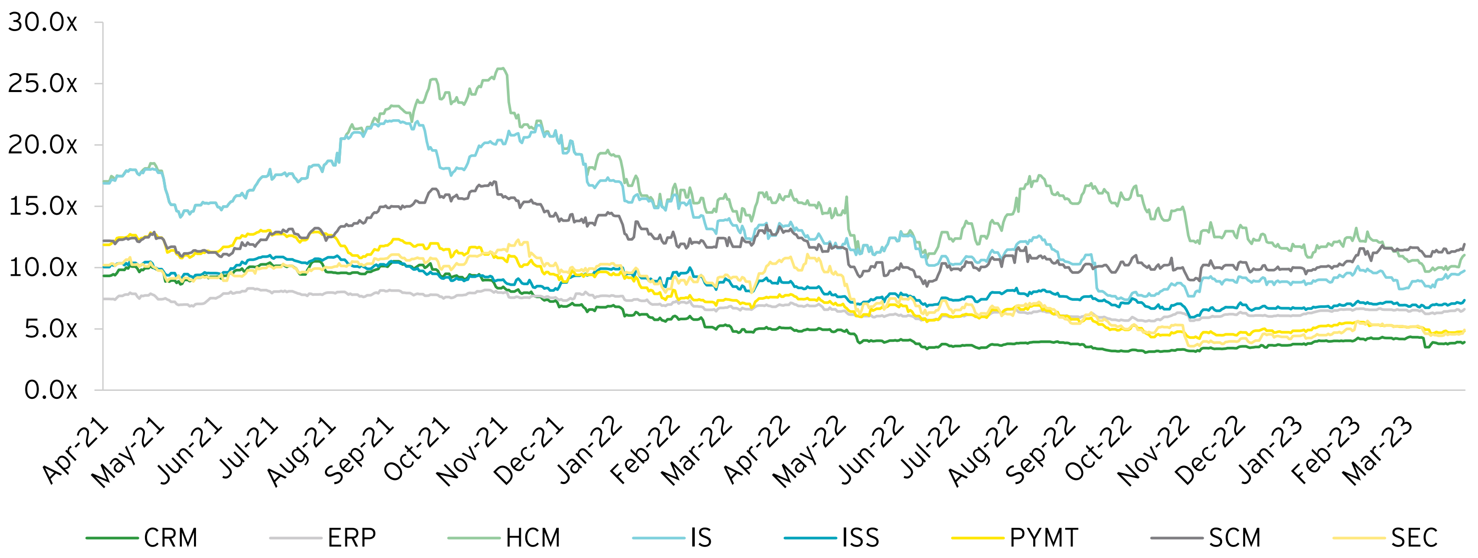

## Deal volume by type of acquirer




## Both deal values and deal volumes have declined in Q1 2023 compared to Q1 2022 levels

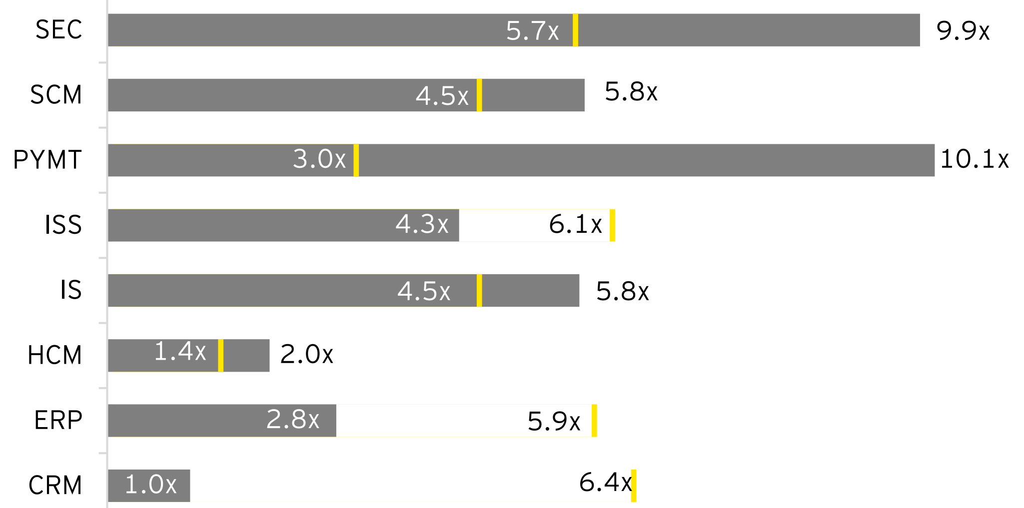



## Public company multiples stayed consistent in Q1 of 2023



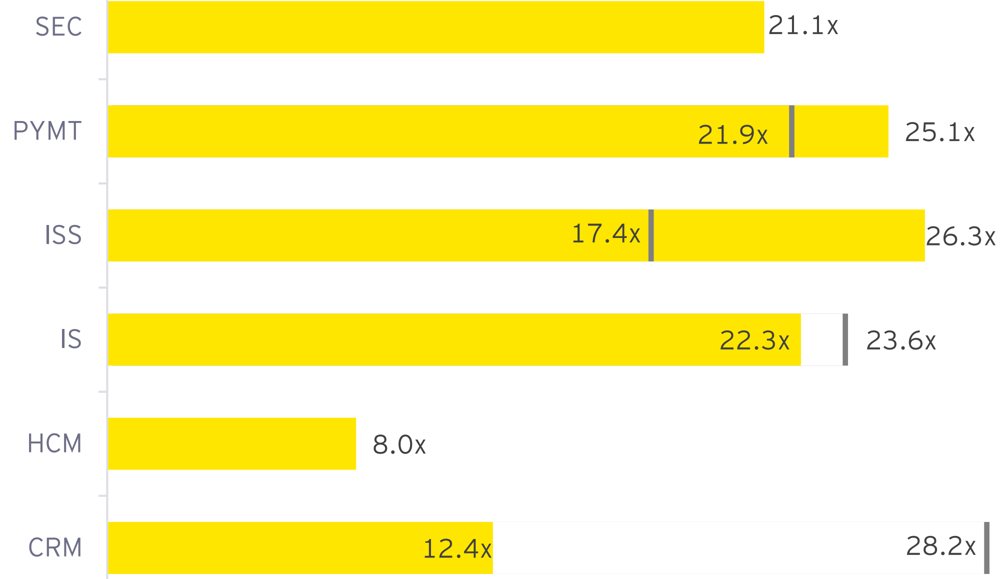

*CRM - Customer Relationship Management; ERP - Enterprise resource planning; HCM -Human capital management; IS - internet Software; ISS - Industry specific software; PYMT – Payment; SCM - Supply chain management; SEC - Security*

## Revenue transaction multiples have remained volatile while some categories have shown an increase when compared to Q1 2022




*Yellow line indicates Q1 2022 comparison

## EBITDA transaction multiples have remained volatile while some of the categories have shown an increase when compared to Q1 2022




*Grey line indicates Q1 2022 comparison

* Sample size for M&A deal multiples has been sourced from S&P Capital IQ and comprises transactions completed between Jan 1, 2019 and Mar 31, 2023 in Canada and the US. The sample has been compiled by EY Orenda Corporate Finance Inc. based on a subjective assessment of transactions in the IT Services sector. Furthermore, the categorization of the sample across various sub-sectors and any analysis thereof, by EY Orenda Corporate Finance Inc. is solely for illustrative purposes and were not created to serve as benchmarks. Every transaction has specific characteristics that impact value and corresponding multiples. It is necessary to understand the background and circumstances surrounding each transaction to extract meaningful insights.

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