The Dealmaker, insight into Tech M&A

Paul Russell is a Corporate Finance Partner at BDO, who has overall responsibility for the TMT Corporate Finance M&A team. Paul spoke to GS-insight with regards to BDO's recent M&A activities, the need for preparation when looking to sell a company and the current state of the market.

What recent M&A deals have BDO been involved in within the technology sector?

BDO has come to specialise increasingly in the technology sector over the past five years. As a firm we are active in a number of different sectors and I think technology is certainly one of the most competitive. We cover both sell-side and buy-side advisory work and we kicked off 2016 advising on the sale of Selection Services for £34.8M to Castle Street Investments as they were creating CORETX, the mid-market IT managed services provider. We followed that in March, working on the buy side with Riverside as they acquired Guestline, a highly specialist SaaS business focused on the hospitality sector. Next we sold a Scottish semi conductor simulation business called Gold Standard Simulation to Synopsys in the US. As the year drew to a close we got even busier and completed three deals. Firstly, the sale OF ITC Secure Networking, a London based IT security services business, to C5 Capital, an international cybersecurity fund. We also sold Medium UK Limited, a specialist value added distributor to Exertis. Finally, we helped Incremental Group Limited raise private equity funding from Maven Capital Partners and acquire First eBusiness Solutions (FEB) Limited.

So 2016 was a good year where we've closed six mid-market tech deals in six different areas, giving a good insight into our capability to advise across various parts of the market. To augment this recent success, we have also hired Robin Brown, formerly EPV of strategy at COLT (using Gillamor Stephens services). Robin has spent his entire career in technology companies, so brings a level of expertise and experience that is unique in our market and enables us to engage with companies at a different level.

What advice do you have for companies looking toward an exit?

Sales processes can really hurt a business so they definitely don't want to start a process in a half-hearted manner. There's a strong chance that kind of approach will fail and a failed process normally sets a business back a couple of years.

Companies aiming for an exit should look to appoint an M&A adviser early on. It can never be too early to have someone talking to you, even two to three years before an exit an experienced advisor will walk a company through the key areas in the business so its ready for the rigours of a process. The joint aims of this exercise are to bring out the positives that will increase value and to understand and counteract any issues that could act as a value drag or even cause the deal to abort. So to execute a smooth process, comprehensive preparation is the key.

How has the world of technology M&A changed over the past couple of years and what, if any, are the implications of Brexit?

The market has been strong for a few years now. There have been certain crises over the last few years such as the Greek debt refinancing, and something along those lines will temporarily take some "air out of the balloon". I have found that the market will probably go quiet when the economy is on the front pages or making headlines in news programmes. This will probably cause people to cite uncertainty as a reason for not progressing with a deal.

Brexit has had a minimal impact. Last year we sold Selection Services, and advised on Guestline. But post Brexit the technology world has continued unabated with Attenda, Adapt, Sabio, Node 4 and Timico being sold and Pulsant buying Onyx. All of these deals have had valuations that you would recognise both pre and post Brexit.

So Brexit hasn't had any detrimental effect?

Brexit has had no impact at all on the deals that were already in progress. The reason for that is because all these businesses are very attractive as investment propositions and there's so much capital looking for a home that people will think "okay, Brexit has happened. I don't know what Brexit means but this is a good business and I need to use my capital." Investors then ask themselves "when will I know what Brexit means? It could be two years or seven years. How long am I going to hold the business for? Five years? I may as well crack on then". Hence processes that were ongoing before Brexit have completed and there seems no diminution in appetite re-new opportunities.

We certainly noticed some quietening off on the part of business owners when the currency flash crash happened in September because the currency news was suddenly all over the front pages of the press. However, the currency has been stable for a few months and hence people aren't talking about it and so M&A activity is pushing forward again. These external factors will come and go and if they're big enough they will cause a mini disruption. If you get enough of them occurring at once you will get a significant disruption where everything will go quiet for a few months. Nonetheless, there's still all that money out there and UK assets are still cheap if you consider them from the American perspective.

Brexit has certainly played well into the hands of some US mid-tier PE firms. However, I don't think this is simply due to the fall in the pound. If you read

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any currency analysis it will tell you that the pound will continue to slide as we become a smaller entity, separate from the European Union, and hence you might end up losing money on an investment over a five year period. I don't think it's to do with an immediate currency gain but rather the fact that US businesses are so much bigger than their like-for-like UK counterparts and can access a lot more in the way of leverage to quickly grow a business. If you multiply a company's size by fifteen times in the UK people say "wow", in America they say "well, fine".

Are there any areas of the technology market that you find are particularly exciting at the moment?

Certainly. I think security is a massive buzzword at the moment, as we have seen first-hand at BDO from working with ITC last year. Companies specialising in security are currently very small and there's obviously a lot of potential.

SaaS also is an area where we can expect further growth. In the case of our deal with Guestline, we saw how they targeted an industry that still used legacy systems and persuaded them to move onto a Cloud model. That, I think, will continue to be a big trend.

There are two big trends currently affecting the services market. One is that the traditional channel, whereby companies sold hardware alongside services, is becoming less and less relevant because everyone is using hybrid Cloud models and hence, as a business, you simply don't need to buy so much kit. We've already started to see businesses who were traditionally very hardware orientated move increasingly towards a software and services based model.

Secondly, the world is changing for data center businesses due to the rise of organisations like AWS and Azure. The smaller data center players simply can't compete with those types of organisations on any metric, be it capacity, availability, energy consumption or price. In order to stay competitive they are going to have to offer more in the way of services. They are increasingly developing an offering based on a hybrid cloud model, wherein they also provide managed services. Even then, people may well move toward entrusting all their data

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to the likes of AWS and Azure as these are the companies spending the most on security. You can never wholly predict how the market will change, it's always in flux, but I think these are some of the drivers that are having a big effect at the moment.