

**IT & Technology
M&A update**
Quarter Three 2023

Lexington's key highlights

Flurry of Private Equity activity during Q3

- The third quarter of 2023 saw a total of 130 deals complete in the UK IT & Technology sector, down from 144 in the previous quarter. This tapering off in deal volumes across the sector is representative of the current overall M&A market sentiment and uncertainty that still looms as interest rates remains at a 15-year high of 5.25%, and ongoing political tensions both in the UK and overseas. However, deal volumes remain significantly higher than pre-COVID levels.
- Q3 marks the first quarter in which Private Equity (PE) tops trade in deal volumes in the sector. This was especially prevalent in the lower-mid market, where of the 47 deals with publicly disclosed deal values below £30m, 36 of these involved Private Equity investments.
- The decline in total deal volume in the quarter also reflects the recent trend seen since 2021 of Q3 delivering the lowest quarterly M&A activity within a full year period. The expectation is that we will see deal volumes reignite as the year comes to a close.
- The buoyant appetite demonstrated by PE in the lower-mid market is an indication that firms are starting to put their available capital to work, having under deployed in the first two quarters, and to take advantage of lucrative investment opportunities in areas such as artificial intelligence, machine learning, and digital transformation. We believe sector appetite remains strong from lower/mid-market PE firms as they can fuel growth and generate attractive IRR/MM returns from tech companies within this size and scale range.
- In summary, despite the recent cooling in M&A activity, expectations are high for deal flow to regain strength as we enter the fourth quarter and ahead to 2024.

Q3 2023 deal volumes matching similar levels seen in Q3 in recent years

Median deal value recovers, suggesting a consolidation of valuations in the sector

Software development and application software remain the most active subsectors in Q3 2023

Private Equity outperforms trade in deal volumes for the first time

Lexington's
IT &
Technology
M&A team



Nigel Griffiths
Commercial Director



Thomas Edwards
Director



Charles Lesbirel
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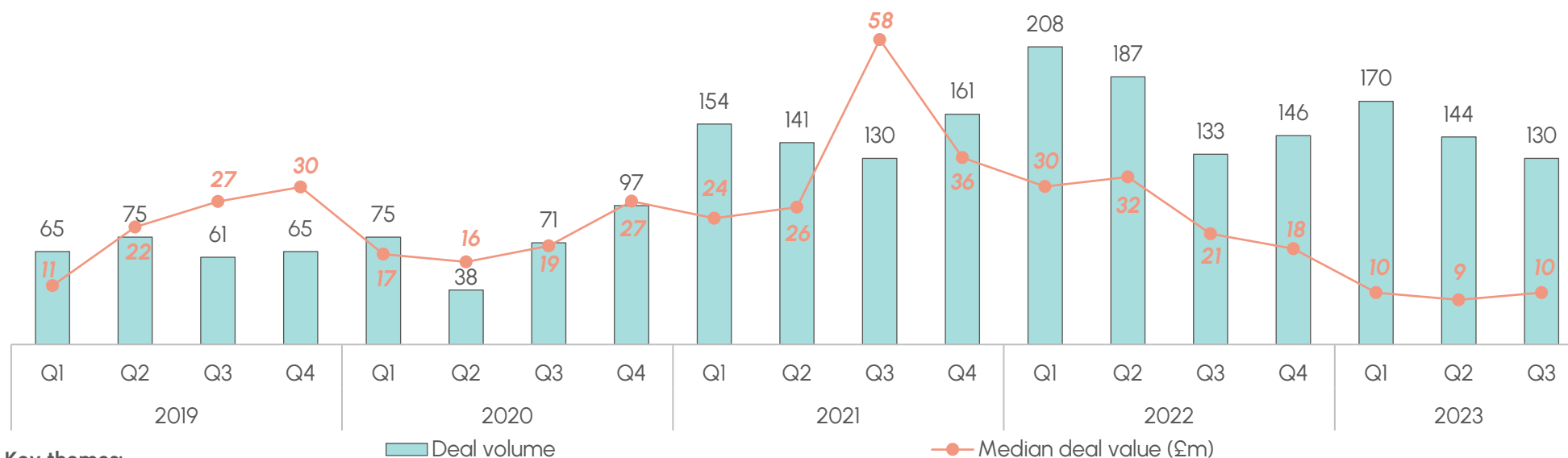
Jade Burgess
Senior Associate



Ioan Brigden
Associate

Quarterly activity snapshot

M&A deal volumes stay consistent with historical third-quarter volumes

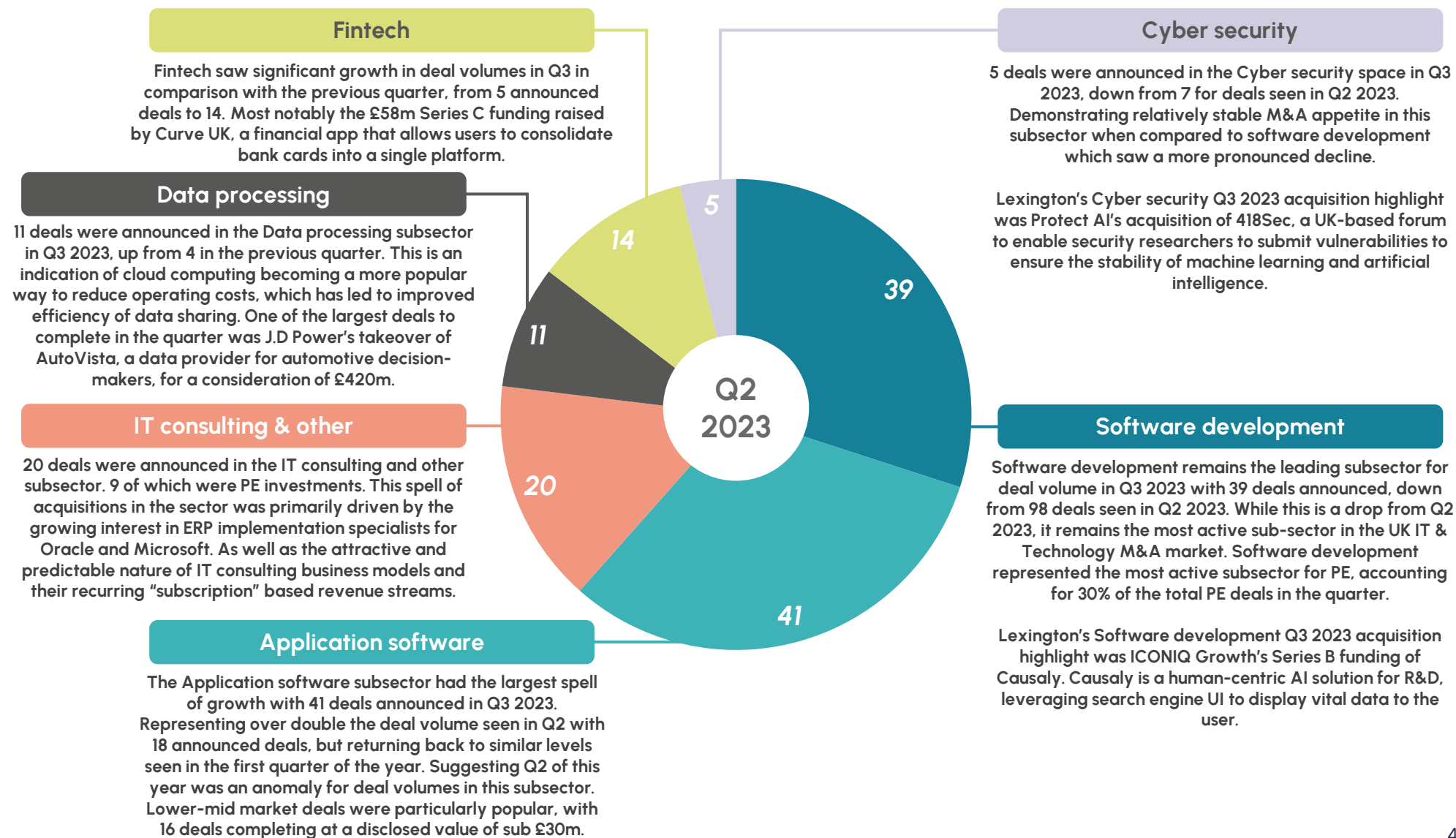


Key themes:

- In the third quarter of 2023 (Q3 2023), M&A activity saw a reduction in deal volume when compared with Q2 2023. However, the median deal value increased by 11% to £10m this quarter. This is a recovery after the drop of value in Q2 2022. Overall, 130 deals were announced in the quarter. Comparing quarters year on year, the first two quarters of 2023 were down an average 20% for the respective quarters, while Q3 2023 was down by 2%. Q3 2023 saw a significant reduction in median deal value in comparison with Q3 2022 and Q3 2021. This suggests that despite a relatively stable deal volume in comparison with these historical quarters, valuation multiples have normalised following an increase during and immediately post COVID.
- Application software investment has seen a significant rise. Portals and platforms powered by AI have seen a particular focus while acquisitions of ERP services have been dominated by Oracle ERP this quarter as Companies focus on either that or Microsoft products.
- Users of IT Consultants are looking to a single IT Service provider to supply the majority of their technology needs. This has been seen through a continued effort from IT Consultants to acquire Cyber Security Companies, coupled with the confidence from PE that have also backed this sector in Q3, giving confidence that Cyber Security will continue to be an attractive prospect.
- The IT and technology sector continues to be a highly attractive area for investment illustrated by the 8% increase in Private Equity deals this quarter compared with Q2 2023.

IT & Technology M&A sub-sector analysis

Application software and software development accounted for over 60% of the total deals in the sector in Q3 2023



Trade v PE

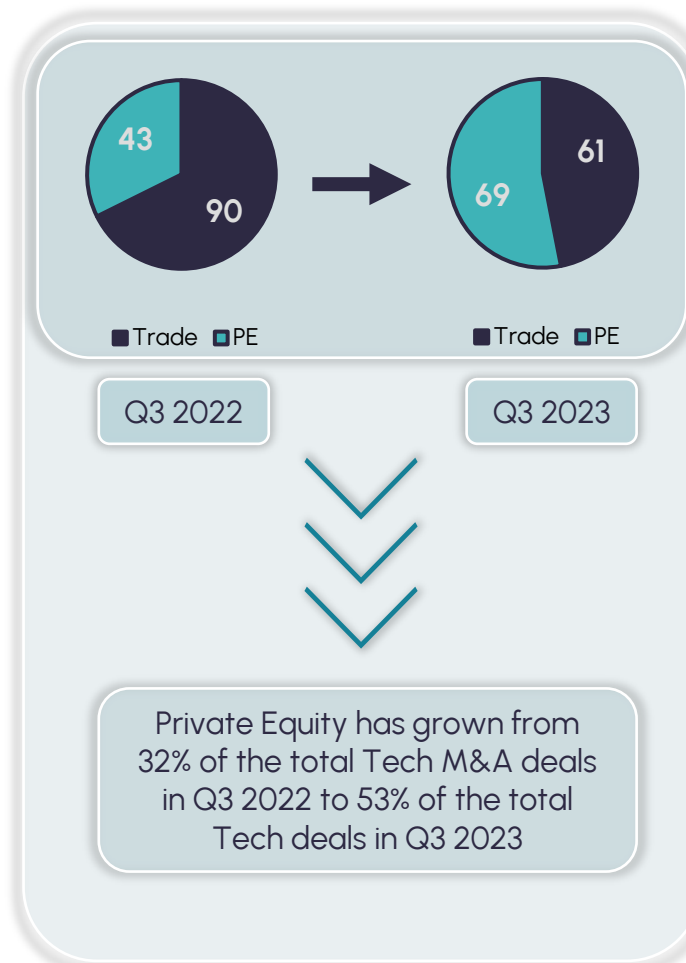
Private Equity transactions surpassed strategic trade deals this quarter for the first time



- In Q3 2023, the UK IT & Technology sector announced 130 deals: 61 strategic trade deals and 69 PE deals. Overall deal volumes have decreased by 10% on the previous quarter but remain above pre-pandemic levels. Despite this decrease in overall deal volumes, we have seen multiples in the sector continue to strengthen as the macroeconomic outlook starts to improve and investor confidence returns.
- Private Equity transactions announced this quarter have increased by 7.6% on the previous quarter, highlighting that appetite in the sector remains strong and long-term confidence among PE investors remains. The higher ratio of Private Equity transactions compared with trade deals in the sector marks a shift from previous quarters. Trade deals, while still robust in number, witnessed a 23% reduction, suggesting macro-economic hurdles possibly constraining trade M&A strategies while the climate remains uncertain.
- During the quarter, Private Equity funds continued to grow portfolio companies through ambitious acquisition strategies. For example, Air IT made their eleventh acquisition in Vital Technology Group since receiving investment from August Equity in February 2020. Other notable Private Equity transactions include the merger of two Oracle ERP companies (NoBlue and Elevate 2) by FPE who went on to acquire a third, BrightBridge, later in the quarter as a bolt on acquisition.
- Despite economic factors faced in the UK during the year, IT & technology remains an active sector for M&A. With strong multiples in the space (page 10), we are optimistic that deal opportunities will start to increase in the coming months, aiding the M&A's market recovery in to 2024.

Strong spell of Private Equity activity

An overview of the most prolific acquirers & investors in Q3 2023



- A flurry of PE activity outperformed Trade in Tech M&A this quarter
- PE M&A activity is at its highest in all quarters since Q2 2022; a 65% increase from Q3 2022 seen this quarter
- BGF, FPE and LDC facilitated 15% of the total activity from PE in Q3 2023
- Oracle ERP saw significant investment as it continues to compete with Microsoft Dynamics

Most active Private Equity in the quarter

BGF, FPE and LDC demonstrated the strongest appetite for IT and technology deals in Q3 2023

BGF



July 2023
Deal type: Series A funding
Deal size: £16m
Subsector: Data processing



August 2023
Deal type: Exit
Deal size: Undisclosed
Subsector: Software development



September 2023
Deal type: Growth investment
Deal size: £4.5m
Subsector: Software development



September 2023
Deal type: Growth investment
Deal size: £4.5m
Subsector: IT consulting

Q3 2023 has been a period of significant IT and technology M&A activity for BGF, with three investments in the sector and an exit of software development specialist, Amdaris. Amdaris had been a portfolio company of BGF's since 2020, when BGF invested £3m in to the company to support its growth trajectory

LDC



July 2023
Deal type: Minority investment
Deal size: Undisclosed
Subsector: Application software



July 2023
Deal type: Reinvestment
Deal size: Undisclosed
Subsector: Application software



August 2023
Deal type: Minority investment
Deal size: £30m
Subsector: Software development



September 2023
Deal type: Secondary buyout
Deal size: Undisclosed
Subsector: IT consulting

Private Equity firm LDC has shown appetite for investments in the application software subsector, with its minority investment in UniHomes, a student accommodation advertising platform. LDC has also reinvested in Evolution Funding, an online auto finance marketplace. LDC then went on to deploy £30m into supply chain technology platform, Sedex, and funded the secondary buyout of Oracle and Microsoft partner, DSP for an undisclosed consideration

fpe



July 2023
Deal type: Growth investment/merger
Deal size: Undisclosed
Subsectors: Software development/IT consulting

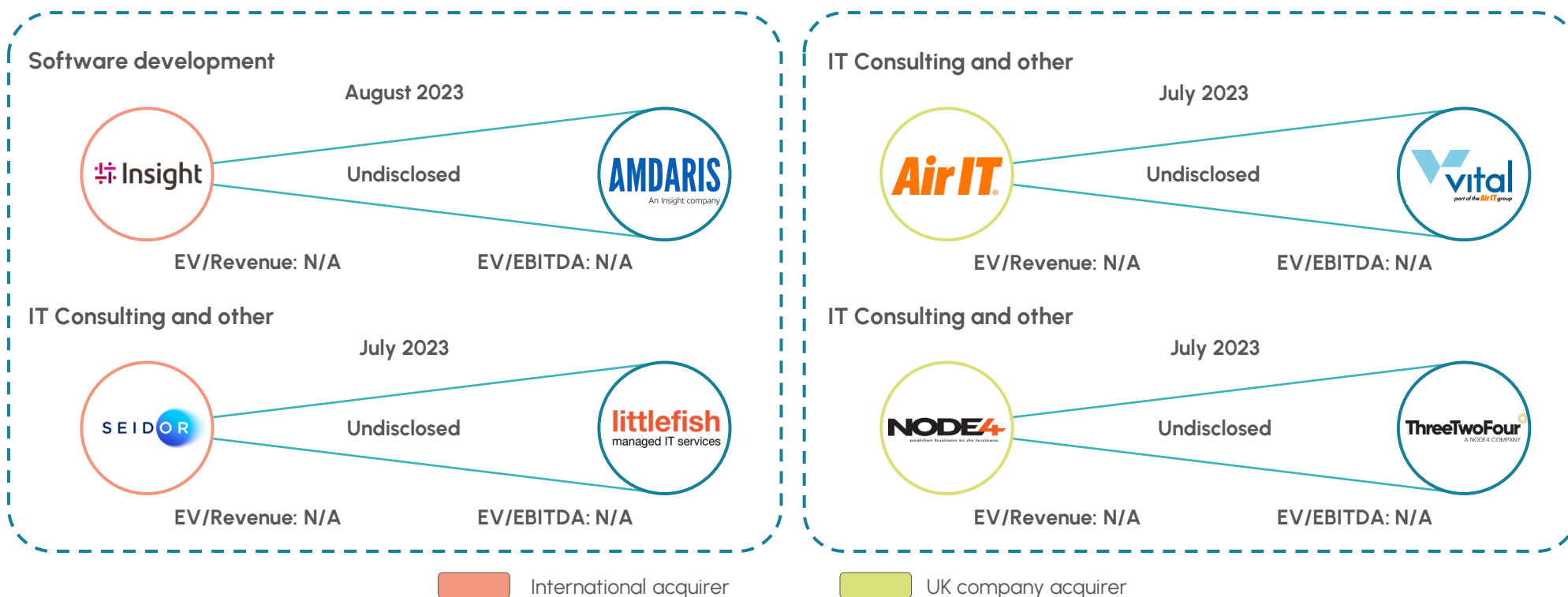


September 2023
Deal type: Acquisition
Deal size: Undisclosed
Subsector: IT consulting

In July, FPE provided growth investment to NoBlue, an Oracle NetSuite and digital transformation specialist. As part of the transaction, NoBlue merged with Elevate2, the largest NetSuite solution provider in the UK, to create NoBlue2. This marked the fifth investment from FPE's Fund III. Later in the quarter, FPE announced NoBlue2's first acquisition, which was of leading NetSuite partner, BrightBridge Solutions, for an undisclosed consideration

Notable transactions – Trade

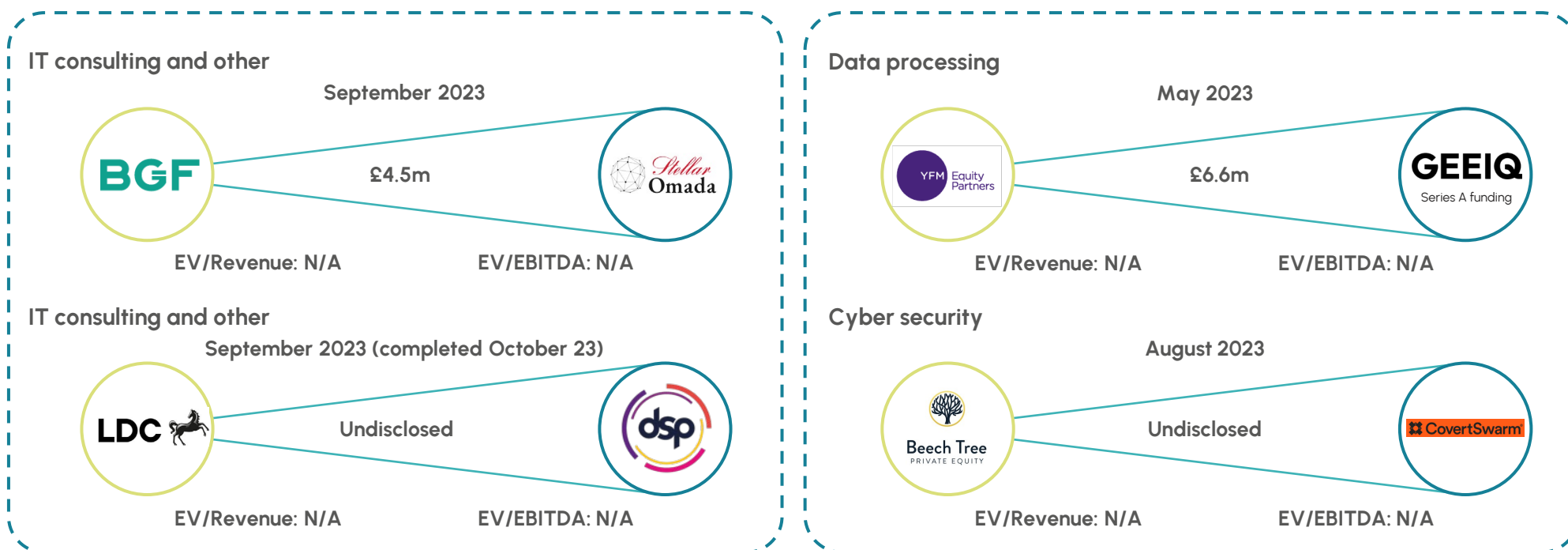
Recent strategic trade acquisitions in the UK IT & Technology sector



- Strategic trade deals dipped by 22% in Q3 2023 compared to the previous quarter with 62 deals announced in the period (Q2 2023: 79). Despite this, activity in the sector remains strong with serial acquirers like Air IT and Node 4 continuing to deliver on acquisition strategies. Trade deals in the quarter also saw large international players such as Insight Enterprises and Sedor continue to build on their existing portfolios and add to their current capabilities.
- Some notable acquisitions in the sector in the third quarter of 2023 include the acquisition of Amdaris by Insight Enterprises, a Fortune 500 solutions integrator, which provided a successful exit for BGF. Since BGF's original investment of £3 million in May 2020, Amdaris has successfully scaled its operations and reported a 94% year-on-year revenue growth in 2022. In July 2023, Air IT acquired IT service provider Vital Technology Group which will add to Air IT's Microsoft cloud solution offering and Node 4 acquired ThreeTwoFour to strengthen its cybersecurity offering.

Notable transactions – Private Equity

Recent Private Equity deals in the UK IT & Technology sector

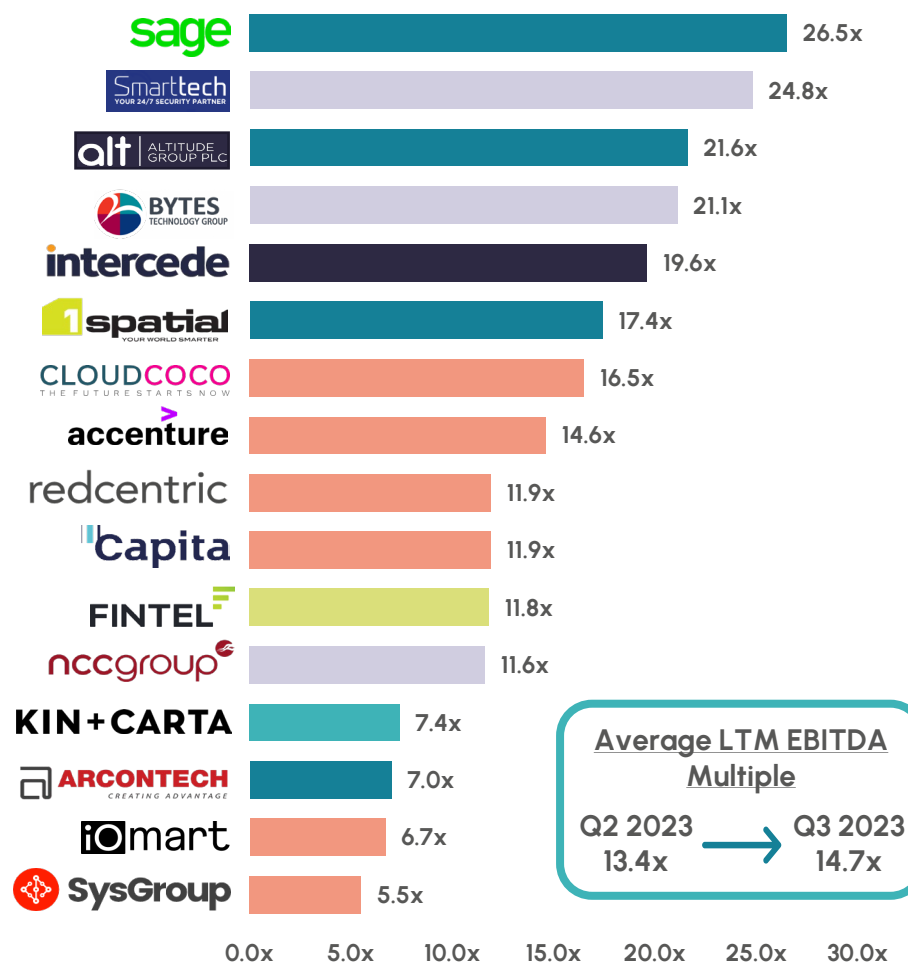


- 71 Private Equity deals/Venture Capital investments were announced in the IT & Technology sector in Q3 2023. The median deal value for Private Equity and Venture Capital transactions was c. £10m, illustrating that Private Equity activity in the lower mid-market remains strong.
- In September 2023, BGF invested £4.5m in Stella Omada, a digital transformation and software testing service provider. LDC also agreed to invest in Database Service Provider Global Ltd which will complete in early October 2023 and provides an exit for YFM Private Equity. This quarter has seen many Private Equity funds realising investments with Foresight Group exiting two portfolio companies, Fresh Relevance and Protean Software. Other exits include HgCapital's exit from Commify UK, BGF's exit from Amdaris Group and Bowmark Capital's exit from Little Fish.
- During the period, GEEIQ, the data intelligence specialist, raised £6.6m in Series A funding round led by YFM Equity Partners. Beech Tree Private Equity invested in CovertSwarm, the cyber-attack simulation testing service provider for an undisclosed consideration.

Quoted company benchmark multiples

The listed companies in the UK that are active in the IT & Technology sector

LTM EBITDA Multiple



● Cyber security ● Software development ● Application software products ● IT consulting and other ● Fintech

Overview

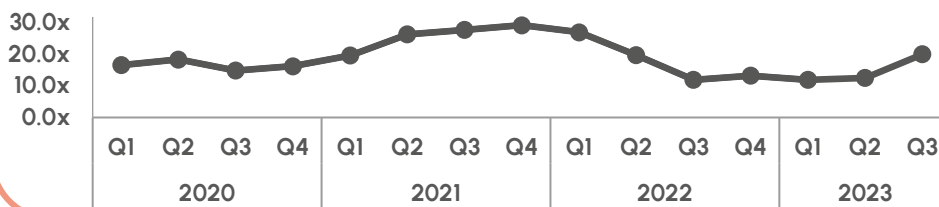
Lexington's has identified 16 publicly traded IT & Technology firms in the UK and Ireland. The data shows that software development multiples continue to exceed the industry average with Sage and Altitude currently trading at 26.5x and 21.6x respectively. Cyber security multiples have also grown on the previous quarter with Smarttech and Bytes trading at 24.8x and 21.1x respectively. The average LTM EBITDA multiple has grown from 13.4x in Q2 2023 to 14.7x in Q3 2023. This increase in Q3 multiples has been underpinned by the impressive growth and performance of companies in the sector this quarter.

Predictions

This quarter witnessed a rise in average EBITDA multiples in the sector with multiples significantly outperforming the general market (see pg. 11). Large market players remained active in Q3, persisting with buy-and-build strategies to consolidate the market and expand their service offerings. We anticipate that as inflation rates in the UK soften and the macroeconomic outlook improves, EBITDA multiples will continue to rise in Q4 2023 into 2024.

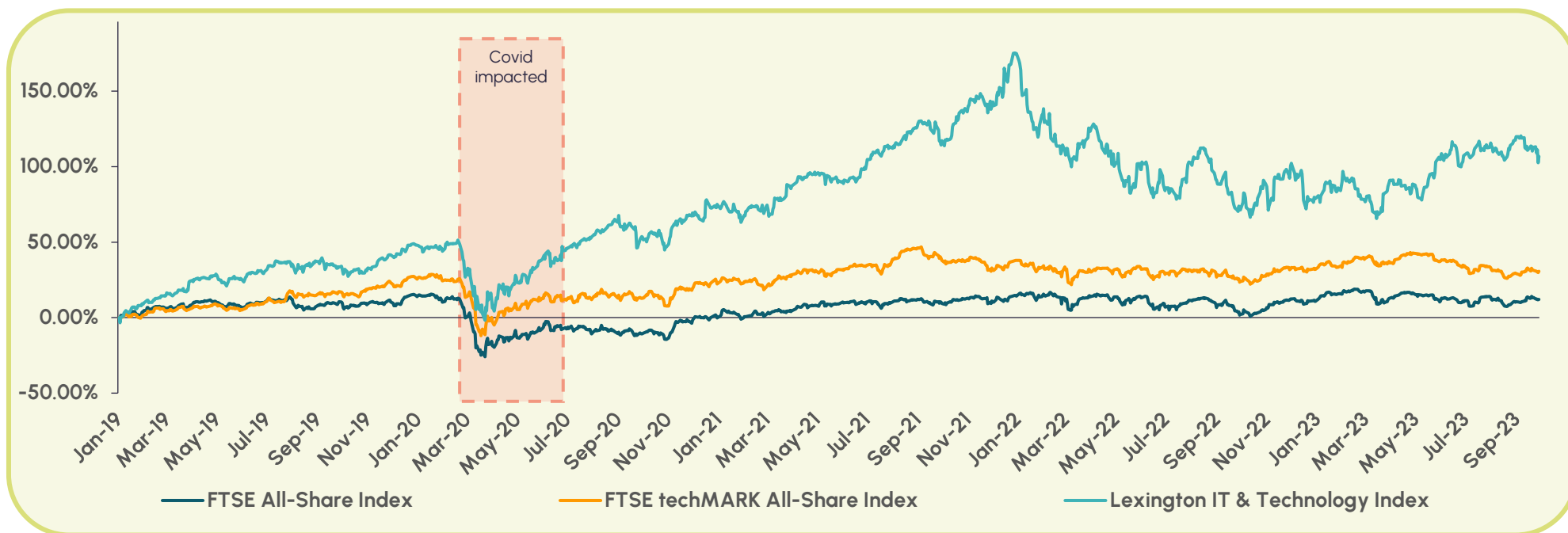
Trends

The graph below illustrates the average EBITDA multiple since Q1 2020 for the quoted companies shown opposite (excluding any anomalies). Despite the increase in multiple, it remains below the peak during the pandemic, at a more normalised level. We expect a gradual rise in multiples to continue as the macroeconomic environment continues to improve.



Tech v FTSE index

The UK IT & Technology industry continue to significantly out-perform the market



- The above graph illustrates how the IT & Technology market has performed against the market as a whole. We have compared the performance of the FTSE techMARK All-Share Index and our own tech index (which includes the 16 quoted companies, see page 10) against the FTSE All-Share Index. The techMARK All-Share Index tracks the performance of all quoted large cap to lower mid-market IT and technology companies included in the Financial Times Stock Exchange Group (FTSE).
- The IT & Technology market has continued to outperform the general UK market in Q3 2023 despite economic pressures in the UK (the cost-of-living crisis and rise in interest rates). Index values for the 16 UK quoted companies mentioned have risen since the last quarter to 102.7% from 98.2% and the FTSE All-Share Index has dropped by 1.1% to 29.9%, compared with a 4.2% rise to 11.87% for the overall market across the same period.

Who we are

Corporate Finance advisory boutique with focus on the IT & Tech mid-market



An entrepreneurial, corporate finance advisory boutique, providing hands-on, trusted advice to businesses, owners and investors with growth, succession and buyout ambitions.

www.lexingtoncf.co.uk



Feedback from the clients we work with

We are really proud of the testimonials we receive from all our clients



Lexington advised the shareholders of Evo-Soft, a Microsoft Dynamics 365 specialist, on its sale to BCN Group

"The BCN acquisition provides a true opportunity for Evo-Soft to continue its growth as a leading Microsoft Dynamics 365 Business Central solutions provider, and represents a huge milestone in Evo-Soft's successful history. Lexington's services have been invaluable to us throughout every step of the sale process, and I'd have no hesitation in recommending them or using their services again."

Ashley McIntyre,
Managing Director



Lexington advised the shareholders of Redcortex, a digital transformation consultancy, on the sale to TPX Impact PLC

"Lexington really helped us through this process, providing invaluable advice at every step and helping make sure we achieved a good valuation for RedCortex. The Lexington team made sure the transaction ran smoothly and kept us informed at every stage."

Martin Britton,
Executive Director and Founder



Lexington advised the shareholders of DevOpsGroup, a cloud services consultancy, on the sale to Amdocs

"Lexington were an excellent corporate finance partner. They took time to understand what support and guidance we needed, and provided invaluable advice throughout the process. The team were professional and easy to work with, always available when needed and the clear and frequent communication throughout, delivered an extremely successful outcome for DevOpsGroup."

James Smith,
Chief Executive



Lexington advised the shareholders of CashCalc, a cashflow planning provider, on the sale to FE fundinfo (backed by HG Capital)

"We're delighted to join the FE fundinfo family and we'd like to thank Lexington for all the work they put into making this happen. Thomas and Pablo were both efficient and effective and we would highly recommend them. Everyone at CashCalc is incredibly excited, so a big thank you from all of us."

Ray Adams,
Director and Founder

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If you would like to learn more about our services and how we can assist you in your growth journey or exit, please don't hesitate to get in touch with any member of our technology team