



M&A Trends 2022

Featuring Eight Key Trends



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Executive Summary

It has been another year of exceptional M&A activity in the Knowledge Economy, with record deal volumes across all geographies, and unprecedented buyer and investor interest in an even greater array of technologies, platforms, and associated ecosystems.

Last year, the Equiteq team presented its first ever M&A trends report, making predictions for the macro and micro factors that would shape buying habits throughout 2021.

In this 2022 edition, we revisit a number of trends to explore their recent evolution and how they will remain strong drivers for M&A in the coming year. From our experience and research over the last 12 months, we have also identified two new trends that will play a critical role in shaping activity throughout the coming year. Most notably, we take a closer look at the emergence of Environmental, Social, and Governance [ESG], which is pushing M&A appetites in new directions as buyers seek to capitalize on the burgeoning 'Sustainability Transformation' agenda.

Among other trends that have crystallized is the broadening of buyer interests across a wider range of emerging and advanced technologies, as well as their partner ecosystems, particularly in the advanced analytics and Robotic Process Automation [RPA] spaces. Nearshoring, too, continues to shape buying habits as firms continue to look further afield to secure business-critical skills in the face of growing demand and ever-tighter margins.

However, the trends in this report should not be taken in isolation. The Knowledge Economy is dynamic, and trends can affect one another, whether Private Equity's growing

ubiquity driving deal volume and market heat, to the broader Cloud adoption trend that continues to underpin everything from more innovative customer experiences and data-driven process enhancements, through to generating demand for skills that push acquirers to look further afield for opportunities.

In this edition, the Equiteq team have also looked to provide actionable steps that both buyers and sellers can take to capitalize on each trend.

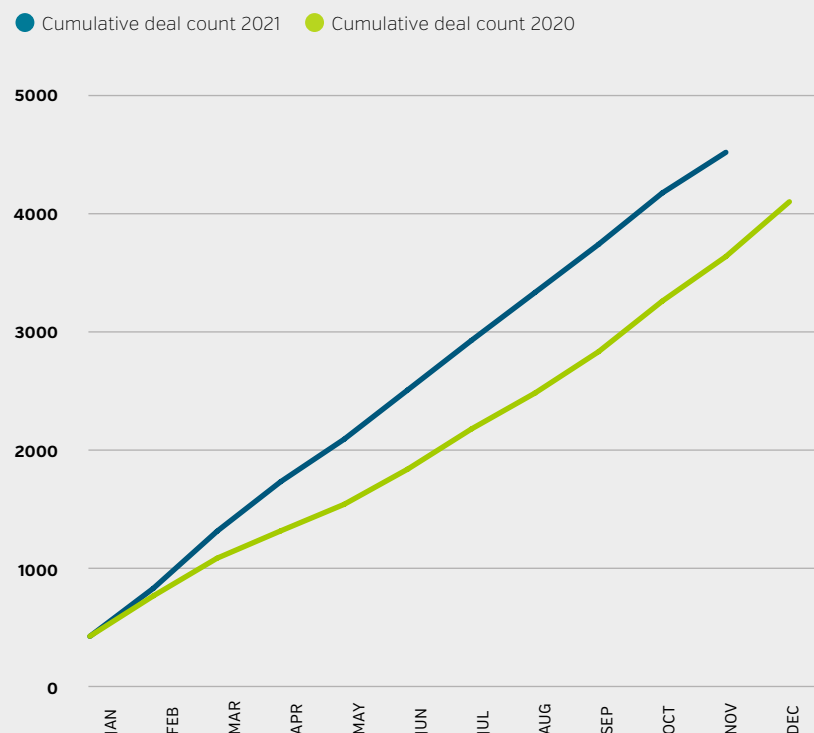
This should act as a baseline for any reader, but equally as an invitation to reach out and discuss further

with a report contributor or member of Equiteq's global team.

As ever, I extend my gratitude and thanks to my colleagues for sharing their invaluable inputs. With M&A activity in the Knowledge Economy higher than it has ever been, both buyers and sellers have a unique opportunity to capitalize during this window. I hope that the ideas within this report enable you to do so.

David Jorgenson
CEO, Equiteq

Running Total of Transactions: 2020 & 2021



Trend 01

The adoption of digital is here to stay

It will come as no surprise to anyone in the space that the adoption of digital technologies, tools and platforms remains a fundamental, long-term trend underpinning M&A activity in the Knowledge Economy. Organizations continue to seek out ways to work more effectively and efficiently in an uncertain world. As a result, Cloud is playing an ever-greater role in enabling entry into more sophisticated areas of technology.

“Fundamentally, we haven’t seen any major changes to the digital adoption trend in 2021 compared to 2020 – all of our predictions still ring true, it’s just the market for digital keeps on getting bigger” says Jerome Glynn-Smith, Managing Director at Equiteq.

With more activity than ever happening through digital channels, we’ve seen a number of adjacent areas of interest emerge among buyers in the last year. Cyber risk has grown, increasing the attractiveness of cyber security capabilities for investors. The long-term Cloud adoption trend is also creating additional demand for development skills capable of building Cloud-ready and Cloud-native solutions.

“Cloud adoption hasn’t changed, it’s a long-term trend,” adds Glynn-Smith. “We’re going through a revolution right now and that isn’t going to change quarter-after-quarter. However, as the core trend progresses, we’re seeing changes arise in the adjacencies that Cloud enables.”

Looking forward to 2022

In 2022, the adoption of digital will persist on its upward trajectory, creating opportunities for buyers across all verticals. Despite efforts to revert back to office-based working, high levels of remote working will continue to accelerate the need for Cloud services and, in particular, the adoption of hybrid-Cloud.

“Spending on Cloud services is only going to grow next year,” says Emmanuel Kostucki, Director



Fundamentally, we haven’t seen any major changes to the digital adoption trend in 2021”

at Equiteq. “Companies are now looking to hybrid-Cloud solutions to take advantage of the lower costs, flexibility, and scalability offered by public Cloud and the greater security provided by private Cloud. Firms that can help clients take advantage of this will be very attractive to buyers.”

However, the greater use of Cloud will almost inevitably raise further concerns around data security. We should expect to see buyer interests in adjacencies like cyber security, especially in the context of networks, data centers and Cloud services, become more acute as a result.

Taking advantage of this trend in 2022

With the demand for digital services – and Cloud services, in particular – growing in the coming year, buyers should look to focus their attention on smaller, more agile firms that possess critical, specialist transformation skills.

“Businesses need people and skills that can help them understand what it means to go through a transformation, whether it’s a cloud migration, the introduction of a data layer, or something else entirely” says Glynn Smith. “However, these are niche skills concentrated in smaller companies, who are better able to recruit this talent compared to bigger firms – and so M&A can help businesses get a competitive edge in this regard.”

Buyers would also be wise to seek out those small firms that already have a presence in popular

ILLUSTRATIVE DEALS

Atos SE acquires
Visual BI Solutions



Kerv Group acquires
cloudThing



ecosystems and a proximity to key vendors, such as Microsoft, AWS, or the emerging analytics platforms outlined elsewhere in this report. Consequently, potential sellers in this space should ensure that they can demonstrate an attractive offering that includes the ability to resell both ecosystem services and wraparound services associated with the consumption of relevant products. ○

Trend 02

Emerging and advanced technologies are being rapidly commercialized

While the technology ecosystem continues to grow exponentially, we have seen the beginning of market movements towards super-specialized, data-driven products that solve specific use cases. From IOT through to hyper-automation via Robotic Process Automation (RPA), there is a growing interest among enterprises for customized software solutions that connect systems in a common data environment. However, end-user maturity remains low, pushing buyer interests towards those niche specialists who can advise, consult and implement a business's journey from "how do we organize and understand our data?" to "how do we use data to drive value?"

As this interest intensifies, we've seen the combination of a growing skills gap and a greater Private Equity presence push multiples for these specialist firms ever higher.

"We're seeing financial investors make platform investments that can act as a launchpad," says Adam Tindall, Managing Director at Equiteq. "From here they can go and acquire other businesses, bolt them on, and roll them up to create something of scale. We've seen this in the data space and we're now seeing it in the RPA space as well."

The growing appetite for Cloud-native platforms (see Trend 5), in the data space especially, is now not only driving buyer activity, but accentuating other predictions made last year. Namely, as the already stark talent and skills gap in the advanced technology space continues to grow, buyers are increasingly looking elsewhere for talent.

"There's so much competition for talent in the advanced tech space, particularly for analytics skills. This makes it extremely hard to scale," says Tindall. "On the one hand, advanced analytics solutions providers are thriving because of the high demand for their software and services. But on the other hand, they just don't have the people to deliver.

In turn, this is pushing buyers to acquire even smaller companies in the search for talent."

But acquiring ready-made skills that enable positive outcomes is not the only solution for buyers. With many enterprise firms acknowledging that with better talent availability they could have generated even more revenue in the past year, we're seeing buyers become interested in companies that can grow and deliver expertise through talent development programs.

"More and more companies are investing in programs that enable them to take people right out of college, or from sectors with adjacent skill sets, and train them up," says Greg Fincke, Managing Director at Equiteq in Boston, USA. "We're seeing this sort of re-purposing and development of talent becoming a major theme and value driver among emerging technologies."

Looking forward to 2022

Heading into next year, the development, adoption and commercialization of advanced technologies is all but assured. However, we may see some changes begin to emerge amid the broader landscape.

"We're starting to see some technology vendors, who have internal professional services arms as a means to help sell their product, essentially winding these down and pushing more into the services ecosystem," says Tindall. "These firms are seeing better results through working with services partners because it alleviates them of the distraction of maintaining functions that may be detractive to the core business. This is likely to drive the demand for services providers among buyers even higher next year."

As demand for services providers and advanced technology ecosystem partners grows, we will see more firms begin to offer vertical-specific solutions as they seek a competitive edge away from industry agnostic solutions. This will provide additional upside on valuation for Strategics that

ILLUSTRATIVE DEALS

MuleSoft acquires
Servicetrace



Microsoft acquires
Nuance Communications



Fishawack acquires
closerlook



Accenture acquires
BRIDGEi2i



are looking for a technology partner in a specific vertical. Alongside the shift towards productization, we also expect to see buyer interests expand as businesses seek further efficiency and more innovative service offerings.

"AI, blockchain, IOT, and mixed reality technologies are all becoming more attractive to buyers," says Kostucki. "This will create opportunities in adjacencies such as data center energy consumption and the end security of value chains. 5G will also create additional productivity opportunities, while we are already seeing companies shifting towards software-defined wide area networks as a result of remote and decentralized work."

Taking advantage of this trend in 2022

We've seen exceptional levels of activity in the Knowledge Economy throughout 2021 and this has only intensified in Q3 and Q4 as buyers try to get deals done before the end of the year. As a result, we may see a drop off in sellers next year, at least during Q1 and Q2.

"With fewer targets to go after, some buyers are likely going to overpay, simply because of the supply and demand difference," says Tindall. "Buyers will need to get ahead of



[Businesses] don't have the people to deliver... this is pushing buyers to acquire even smaller companies in the search for talent"

competitive processes and position themselves more effectively. This means pushing for more corporate development horsepower to be able to go and build relationships with nascent, fast growing, technology services companies to avoid losing out on deals."

With buyers often struggling to articulate the benefit of a deal to sellers, especially when the area of interest is still emerging, it is imperative that acquirers work on being more tactical, more thoughtful, and more relationship focused in order to succeed next year.

For sellers, growing skills gaps are an opportunity in which they can

differentiate and attract interest.

However, with growing numbers of both Millennials and Gen Z employees in the workforce, this means rethinking their approach to talent.

"Buyers want skills, so any seller that can put together a compelling employee value proposition that attracts and retains talent will be very attractive," notes Fincke. "We're seeing more and more clients rethinking their approach to employee engagement just to stem the tide of talent loss. You need to be able to show that you can hire juniors and turn them into billable resources quickly. If you can get this right, you'll undoubtedly see interest from buyers."

Buyer interest across digital technologies

From Global Buyers Report 2022

Private Equity Strategic Acquirers

Data analytics



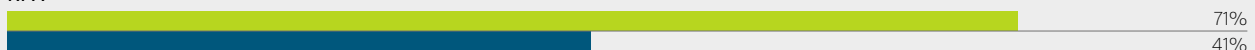
AI/ML



Cloud computing



RPA



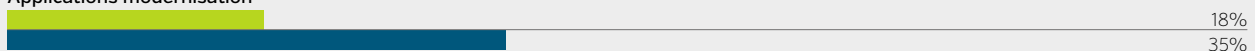
Cybersecurity



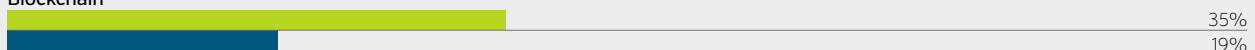
IoT and connected systems



Applications modernisation



Blockchain



Trend 03

Tech-driven enablement of customer-centricity has arrived at the center of consulting and tech-enabled services propositions

Prevalent amongst the drivers – and outcomes – of rapid, organizational digital transformation over the last decade or so have been dramatic changes to consumer expectations and behaviors. As consumer-facing firms look to respond to these – directly, and through developing dynamic capabilities to be more adaptive to future change – we've seen the prominence of the customer journey and experience as an axis of development and innovation on the rise.

For years, data-driven insights have been providing a new 'fabric' to knit together ever more personalized customer experiences. What has gained ground in 2021 – and looks set to influence 2022 and beyond even more heavily – is a widespread acceptance among firms consulting into the C-suite that delivery of customer outcomes through that ever more sophisticated customer journey, should now be central to their proposition. With an impetus to achieve this at depth, scale, and with inherent complexity, consultancies are rethinking their inorganic strategies.

"Changing customer behaviors, experiences, and expectations – all driven by accelerating digital transformation – are having a serious impact on M&A strategies for consulting and tech-enabled services firms. It's driving the appetite for businesses that have domain expertise in transforming connectivity with the customer," says Paul Dondos, Managing Director, Global Buy-side & Market Intelligence at Equiteq. "Firms want to be more responsive. They want an infrastructure that's more effective in selling to customers and that will improve the consumer experience.

And, with innovation running at pace, training and hiring the talent to deliver this is only part of the answer: hence the M&A."

Consequently, we're seeing an acceleration of acquirer and investor interests to accommodate these shifts in consumer expectations in terms of engagement and interactivity. As the pandemic shock recedes, businesses are gaining a deeper appetite to cater to this level of consumer change. At the vanguard, we've seen Accenture act at pace by ordering 60,000 Oculus headsets that will help generate next-gen consumer strategies. The firm has already partnered with Kellogg's and Qualcomm to develop a Virtual Reality (VR) solution that uses eye tracking to provide accurate and unique market research.



Changing customer behaviors, experiences, and expectations – all driven by accelerating digital transformation – are having a serious impact on M&A strategies for consulting and tech-enabled services firms"

Looking forward to 2022

So what comes next? Evolving buyer interests suggest the standout opportunities will lie with the most novel technologies going forward.

"In 2022, we're going to see even greater developments in the customer experience as buyer interests propel a synthesis between the evolving channels between business and consumer," says Dondos. "Virtual Reality [VR] and Augmented Reality [AR] are accelerating. The Metaverse has gone mainstream. Translating that change into risk and opportunity for companies that serve consumers and then forming and implementing initiatives to respond to these is becoming more demanding - and at a rate that defies remedy by organic growth."

An increasing part of those 'initiatives to respond' will be software, and consumer technology companies are also engaging in M&A as a means to rapidly develop their own capability. But besides software acquiring software, technology businesses are also now looking to deepen their market reach and relevance by adding domain-specific service capability in order to reinforce their connection to their customers. Expect further convergence of this nature [software acquiring services to deepen domain expertise] in 2022.

Taking advantage of this trend in 2022


The implications of this trend are clear for all parties in the coming year. Buyers should look to impress upon sellers a clear story that emphasizes the variety and depth of mutual opportunity presented by the continual development of consumer needs and behavior.

With enterprise retail businesses needing to expedite changes to their fundamental operating models to accommodate these new behaviors, both software and services firms have a clear opportunity to support such transformation. Accordingly, any business with the components and means of delivery for solving challenges presented by those evolving consumer habits and needs will likely be seen as a potential target.



Both buyers and sellers have a huge opportunity to capitalize in the consumer space during 2022"

"Both buyers and sellers have a huge opportunity to capitalize in the consumer space during 2022," says Dondos. "Neither services nor technology firms can always be nimble enough to cater organically for rapidly changing customer needs. But in combination large and small firms can achieve outcomes of greater scale and

impact than either could otherwise, with cutting-edge, higher focus capabilities being leveraged across a broader platform. Both sides of an M&A combination can lean into that shared opportunity - and consumers can look forward to the benefits of continued, high-velocity evolution of their interface with business." 

ILLUSTRATIVE DEALS

PayPal acquires
Paidy



NortonLifeLock
acquires Avast



WPP acquires
Velvet Consulting



Accenture acquires
HRC Retail Advisory



Trend 04

Private Equity participation is still increasing

Given the M&A activity we've seen in the Knowledge Economy over the last 18 months, it may sound almost quaint that an increase in Private Equity participation wasn't considered a given. Yet, here we are, and - as evidenced by the findings in our 2022 Buyers Report - this trend has only further solidified.

An excess of dry powder has driven ever greater levels of PE activity as financial investors have grown increasingly comfortable with the value Knowledge Economy businesses can offer. The triptych of software, services, and advisory, wrapped together to deliver sticky, recurring revenues are a clear and enticing prospect for any PE willing to pay the multiples the market currently demands.

However, while we suggested last year that PE could miss out on emerging tech opportunities to Strategics, due to a lack of adoption and unclear profitability, we've actually seen financial investors grow in confidence when it comes to innovative technology.

"Private Equity have seen enough now to understand that if you're really good in a specific space, then they can afford to be more comfortable betting on the technology," says Fincke. "Take the automation space; if you're the best UiPath partner then you're going to keep getting work in that ecosystem. Before, PE firms would have looked at this project-based approach and asked where the next piece of work is coming from. Now, they better understand that if you're best of breed and tightly aligned to a technology platform, then you're going to keep getting work. This makes

them feel much more comfortable that it's a less risky investment."

Looking forward to 2022

The increase in PE participation pervades multiple trends in the Knowledge Economy. While we expect activity to remain high, the biggest obstacle to this is the risk of rising inflation and its impact on interest rates. If debt becomes more expensive as a result, then this could make it harder for PE to be as competitive on deals in our currently overheated market.

However, such impacts may be limited to only certain sectors, suggests Tindall. "Inflation is unlikely to impact all sectors the same. It's going to have more of an impact on the sectors where higher than average ratios apply to deals versus the Knowledge Economy where Private Equity would normally take 3x EBITDA out versus 6x-8x on a recurring revenue business that has assets on its balance sheet."

In fact, with financial investors needing to put money to work, we may actually see inflation push PE funding across a broader spread of sectors.

Taking advantage of this trend in 2022

With PE's appetite for Knowledge economy firms growing, investors looking to play in the space will need to find the People businesses that are not only best of breed but have figured out how to scale.

"Ultimately, if you want to deploy capital in the knowledge economy, you need to be clear that not all companies are created equal," concludes Fincke.

39%

of Private Equity investors say growing market heat has increased their participation in Knowledge Economy M&A

ILLUSTRATIVE DEALS

Vista Equity Partners acquires Blue Prism


VISTA
EQUITY PARTNERS

blueprism®

Baring Private Equity Asia acquires Tricor Group




BPEA
Baring Private Equity Asia

tricolor

"The ones that can grow and scale are the ones that are going to be the winners - and provide the most successful exits for Private Equities." 

The impact of market heat on buyers' plans

From Global Buyers Report 2022

 Increased participation  Reduced participation  Had no impact



Private Equity



Strategic Acquirers

Trend 05

Next-gen technology platforms are coming of age

The acceleration and evolution of Cloud, especially among enterprise-level companies, continues to shape the adoption of next-generation tech platforms. The growing demand for accessible data and analytics is also fueling the attractiveness of emerging, Cloud-native platforms that can simplify the way companies can interpret, interact, and utilize data.

"Cloud-native platforms are a growing component among enterprise-level businesses because they can provide not only greater insights, but also steadier revenue streams. Both offer greater resilience during a potential crisis," says Kostucki. "Yet, these platforms still require a number of custom integrations that rely on partners to create and service."

As the adoption of Cloud-native analytics platforms such as Looker, Snowflake, and Alteryx grows, so the surrounding partner ecosystems become more lucrative. With platform-relevant talent, skills, services and integration providers growing in demand, the competition among buyers has pushed the price to acquire such capabilities ever higher.

"It's having a real impact on demand," says Fincke. "We're hearing growing concerns from Strategics in the space about losing to PE that will overpay. This is creating situations where Strategic buyers are having to readjust their calculations, recognizing that they may have to wait for a PE to exit in order to find anything of scale in certain key platform ecosystems."

Looking forward to 2022

The appetite for Cloud-native platforms - and especially analytics platforms - will only grow in the coming year, so competition for the most valuable ecosystem partners will further intensify.



Organizations are going to have to reconstruct their environment to be more efficient. This presents a huge opportunity for Knowledge Economy firms to help ... both strategically and technologically"

An area in which we may begin to see M&A opportunities emerge in 2022 is the rationalization of tech within enterprises. After 18 months of adopting as much technology as quickly as possible to move into a digital environment, organizations are starting to find themselves in a position where they can take stock of what they've invested in, find out what really works, and identify how these platforms and tools work together from a cost and efficiency perspective.

"I would suspect that many enterprises probably overspent on technology solutions that they don't need in the last year," says Fincke. "Now that could be seen as a negative for our clients, but it's also a positive because it means these organizations are going to have to reconstruct their environment to be more efficient. This presents a huge opportunity for Knowledge Economy firms to help companies navigate the rationalization of platform investments both strategically and technologically."

ILLUSTRATIVE DEALS

Rapid7 acquires IntSights
Cyber Intelligence



Sapphire acquires
Opal Wave



Zoom Communications
acquires Kites



Atos acquires
Cloudreach



Taking advantage of this trend in 2022

With the rationalization of platforms on the horizon, picking the winners and losers among ecosystems will be critical for buyers in 2022. Currently, the market remains in the phase of the cycle where the number of solution providers continues to grow. This means that picking the right bet remains an open question. As a result, buyers must look to enterprise-level adoption, the Fortune 500, and even established platforms for an indication of where the market is heading.

"Buyers need to be aware of the technology platforms that are being rationalized, because if you're wedded to a particular technology that is losing favor then you're going to have an issue," says Tindall. "Take the automation software provider, Blue Prism, for example. Industry consensus suggests that Blue Prism is probably going to lose market share to other, emerging pipeline automation solutions. This means that potential investors ought to diversify their focus away from Blue Prism and instead look to up and

coming technology solutions, such as UiPath instead."

It's worth noting though that while paying attention to emerging platforms is key, buyers ought to keep one eye on the potential resurgence of established platforms too, with the SAP ecosystem being of particular note. Despite extensions to its support for legacy software (with SAP pushing this deadline back to 2027), now is an interesting time to be a services provider in the SAP ecosystem as Strategics scramble to secure the capabilities required to support legacy software and necessary migrations.

"All of a sudden SAP companies are in high demand because buyers didn't see this coming," says Fincke. "Now there's a huge demand for SAP capabilities. The last thing a Wipro or an Accenture wants to do is lose a core ERP implementation because they don't have the tech or the people - that's the sort of thing that could cost them tens of millions of dollars in direct or indirect project work. So, for any sellers in the ecosystem that are thinking of transacting - now's the time to get your house in order and act." ◉



Buyers need to be aware of the technology platforms that are being rationalized, because if you're wedded to a particular technology that is losing favor then you're going to have an issue"

Trend 06

Vertical software solutions continue to play a growing role

Many of the trends in the Knowledge Economy are long-term, playing out over multiple years. One such persistent trend is the growing attractiveness of vertical software solutions.

We've seen buyers continue to look beyond the ecosystems of popular, horizontal software solutions in the pursuit of opportunities in smaller, less competitive industry verticals. Against the backdrop of uncertainty that has dogged global business for almost two years, bolting-together firms to create a market leader in a niche vertical is clearly still appealing - and increasingly so to Private Equity. With PE participation in the tech-enabled services [TES] peaking in Q3 2021, we should expect the long-term, sticky, and recurring revenues of such a software play to continue attracting financial investors going forward.

Yet, with vertical investment growing in popularity, we're now seeing PE begin to invest in large, second tier horizontal players too. By taking these firms private, buyers are looking to expedite the modernization process and jumpstart the route back to top-tier success. Clearlake Capital's \$5.2bn acquisition of Cornerstone on Demand, a specialist talent management software provider albeit one currently lagging behind top tier firms such as Oracle and Workday, is a clear example of this.

Looking forward to 2022

As we head into 2022, we can be confident of the verticalization trend continuing in the same vein. The interest of PE and PE-backed acquirers in niche software solutions are unlikely to fade, although this may depend on the severity of changes to Capital Gains Tax [CGT] rates in the US as well as potential inflation, the specter of

which has loomed just over the horizon for what seems like the better part of 18 months now.

"At some point interest rates are going to go up and debt won't be as cheap as it is now. It won't be as easy to get and it'll have some impact on Private Equity's ability to be the acquirer of choice," notes Jeff Becker, Managing Director, Head of M&A - North America at Equiteq. "Now, that doesn't mean that we'll see PE go away and PE-backed companies stop acquiring. But we could see the heat cool a little, restoring the equilibrium and helping Strategics get back to equal footing."

Yet while CGT increases may stem the tide of activity and inflation remains a possibility, as things stand, with so many active financial investors in the space right now, it's hard to see a major deviation. So, while inflation could potentially benefit Strategics in the mid-term, it's unlikely that we will see them as the more active acquirers of niche vertical software solutions firms anytime soon.

“

At some point interest rates are going to go up...and it'll have some impact on Private Equity's ability to be the acquirer of choice [which could help] Strategics get back to equal footing”

ILLUSTRATIVE DEALS

Microsoft acquires
CloudKnox Security

CLOUDKNOX

Clearlake Capital Group
acquires Cornerstone
OnDemand

CLEARLAKE

Thoma Bravo
acquires Medallia

Medallia

Specialist Resources
Global acquires Quovantis
TechnologiesSpecialist Resources
Global

Quovantis

Taking advantage of this trend
in 2022

With PE investors flush with funds, now is the time for sellers who are thinking of transacting to avoid overthinking.

"Don't be too cute," says Becker. "Get ready now, do everything you can to prepare: get your financial data, your management team, your financial team in order. Don't wait until the last minute because the markets could start to change, and they are the one thing you can't control."

Preparation and agility are the name of the game at this moment in time. Whether it's interest rates or activity cooling in the wake of CGT increases, vertical software solutions providers that want to play a role while this trend is still in the ascendancy ought to hit the market sooner rather than later. This means being ready to press the button when a buyer shows suitable interest - and if you're doing something right, they will.

Acquisition priorities
by vertical sector

From Global Buyers Report 2022

- Healthcare and Life Sciences
- Financial Services
- Retail
- Energy
- Heavy Industries
(e.g. Manufacturing)

Due to rounding figures
may exceed 100% total

First priority

22%

38%

12%

12%

16%

Second priority

24%

15%

15%

29%

18%

Trend 07

The need to acquire nearshore skills is becoming more acute

The nearshoring trend continues to gather pace, with many of last year's assertions having completely played out. The ongoing shortage of skilled labor in critical areas, especially in the IT space, has only exacerbated buyer motivations to solve skills gaps through the acquisition of firms in LATAM, Eastern Europe and Southeast Asia.

"What's especially attractive about these regions isn't just the fact that they're nearby, in the same time zone and have some degree of cross-cultural compatibility - it's the cost arbitrage," says Daniel Siller, Managing Director at Equiteq in New York, USA. "This is increasingly apparent and it's diversifying the countries of interest for buyers. Mexico has been a popular nearshoring destination in recent years. But we're now seeing countries like Colombia and Guatemala gain buyer interest. Not only are the skills the same but the lower labor costs enable firms to triple or even quadruple their margins."

With the demand for IT skills inflating wages, buyers need a way of offsetting ever tighter margins. In all corners of the globe, this is driving the acquisition of nearshore firms that can leverage low-cost services and skills in local markets - particularly on a project-related basis - to support clients globally.

"Countries like the Philippines, Indonesia, and Vietnam all possess high quality data engineers. This is making them highly attractive to buyers looking to serve clients in Asia, as well as the US and Europe," says Sylvaine Masson, Director, M&A Services for Equiteq in APAC. "The most interesting firms in the region have been those that not only have the skills ready for deployment, but who have been able to demonstrate effective internal training and talent development processes. This is highly attractive in the face of a global scarcity of expertise."

Looking forward to 2022

As organizations look to both redress tighter margins and acquire business-critical skills, we are seeing nearshoring M&A activity spread to new regions, especially among North American buyers. Countries like Costa Rica and Guatemala are increasingly being considered, while Brazil and Argentina are both becoming key centers within LATAM. Both boast a growing population of larger, more developed companies as well as a depth of IT services that makes opportunities immediately attractive. As the popularity of these countries grows, we're now starting to see buyers look beyond primary cities for skills.

"The resources in larger cities are becoming exhausted due to the increase in demand and M&A activity," says Siller. "So, operators are switching their attention away from resources in larger cities like Buenos Aires, São Paulo, or Rio. They're starting to look towards secondary cities to find more abundant and less expensive talent while tapping into IT talent pools directly from universities."

With the arbitrage so compelling from a pricing perspective, the economically attractive models on offer in these emerging nearshoring regions means that Private Equity firms are entering the fray in greater numbers too. This will likely lead to consolidation within markets as PE firms start to sponsor roll-up strategies.

"We are seeing PE being very deliberate about putting together pieces that they know are valuable," says Siller. "You've got the 'geography' piece, but you've also got the 'access to end market clients' piece. So, while not all firms in LATAM may serve foreign markets, acquirers can quickly redeploy that local talent to service higher margin projects in higher margin countries. By assembling the right pieces, financial investors will be able to

ILLUSTRATIVE DEALS

EPAM Systems
acquires S4N

<epam>
S4N

intive acquires
Spark Digital

intive
SPARK
DIGITAL

Globant acquires
Atix Labs

Globant
//ATIX
LABS

provide services to the market that provides them with the biggest arbitrage in terms of cost and talent. The IT services company, Globant, is a good example of this - they're the reference point for what can happen when the pieces are assembled well."

However, while such opportunities are appealing, there will come a point

ILLUSTRATIVE DEALS

Perficient
acquires Izmul

PERFICIENT
IZMUL

Roam Digital
acquires Amdocs

roam
amdocs

when the nearshore competencies start to run dry, with available talent having already been acquired. Depending on activity next year, we may see buyers start to diversify and look to APAC for resources to serve LATAM, while Latin America services North America. This hybrid offshore/nearshore interplay will be primarily driven by situations where talent constraints force buyers to look further afield for the skills required to enable rapid growth.

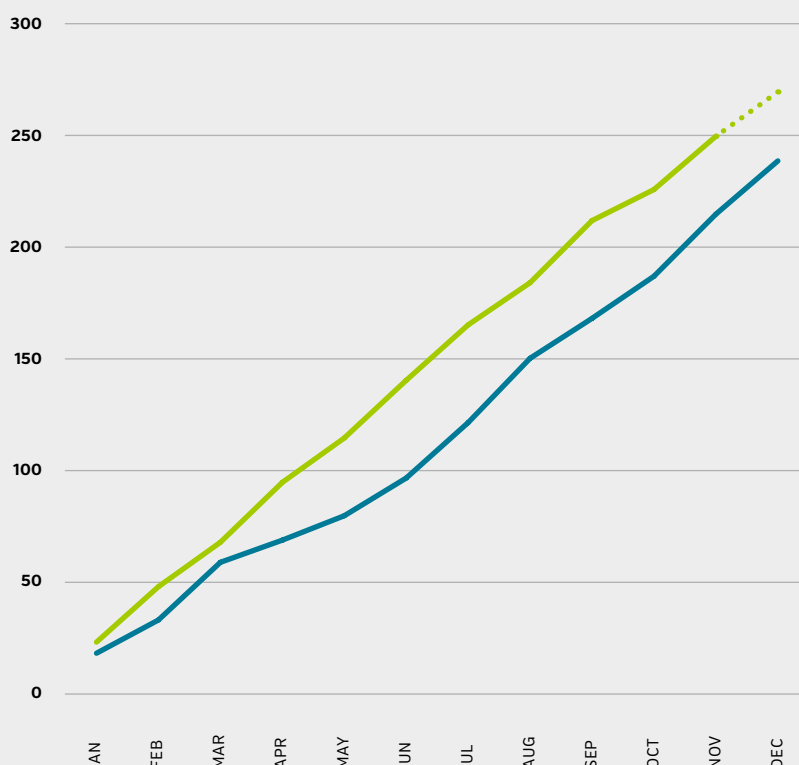
With talent still so scarce, the nearshoring trend is creating a favorable market for sellers. Good assets that can demonstrate growth or proprietary methodologies, will continue to trade at a significant premium in the coming months and beyond.

"We've seen asset evaluations increase by more than twenty-five percent - the dynamic is completely abnormal. This has been created purely by the demand for digital transformation and a lack of abundant talent," says Kostucki. "However, we've also seen a lot of good assets transact in the past year. So, although buyers may want to be selective, a growing

Cross-border deals are growing in volume as buyers look abroad for vital skills

● 2021* ● 2020

* Estimated to year end



scarcity of assets will likely prove inhibitive. The reality of this is that even second and third tier firms are going to start transacting at higher multiples."

Taking advantage of this trend in 2022

For buyers looking to make acquisitions in geographies they are perhaps less familiar with, it is vital to remember two words: 'patience' and 'partner'.

"Buyers need to partner with advisers who understand the system, who understand the players, and who understand the risks in the region," says Siller. "They also need to make certain that they have a viable, tested acquisition

strategy. Having both a strategy and patience is vital. You need to know that the individual pieces of a prospective roll up exist, you need to know how you're going to go about making those acquisitions because there can be substantial legal and cultural differences from country to country within the same region, which makes transacting in each one fairly different."

Sellers, too, can benefit from partnering with experts from bigger markets. This will help them to assess their offering against buyer demands, but also identify where changes could be made to enhance their story and make themselves a more viable acquisition. ○

Trend 08

Sustainability and ESG are climbing the corporate agenda

With global policies facilitating the sustainability agenda, ESG has rapidly ascended the list of Boardroom priorities over the last year. 'Sustainability Transformation' now has the potential to quickly become the new digital transformation. As such, those businesses that can help firms to abide by legislation such as the EU's 'Sustainable Finance Disclosure Regulation' are increasingly valuable - not least because of the predictable revenue streams they promise. In turn, the early adopters of this new kind of stakeholder capitalism will likely prove to be winners.

During the year, Private Equity has continued to raise significant funds targeting ESG assets, typified by KKR, who took control of ERM in May with a strategy to build the world's largest pure-play sustainability consultancy. We've seen these Private Equity-backed players carry on building up over the last few quarters, making regular, small acquisitions. Meanwhile, companies with ESG credentials have also been high on the list of targets from SPACs, with strong institutional demand encouraging a wave of new sustainable investment SPAC IPOs.

In the face of this competition, Strategics have been incisive in the way they've entered the sustainability/ ESG space through M&A, acting resourcefully to identify carve-outs and minority investment opportunities with a critical eye for transactions that they can win.

"To be able to gain access to this space, we're seeing Strategics turn to making minority investments in order to leverage the sustainability capability from an investee into their organizations," says Dondos. "They're making investments that could - and probably will - pay off given the demand for these assets, but they're

also getting the benefit of absorbing that sustainability capability into their organizations - and that's significant."

In many ways, the evolving ESG space is evocative of the digital incubators set up by the big consultancies over the past decade, wherein vehicles such as Accenture Interactive and Deloitte Digital enabled firms to not only enhance their service offering by acquiring capabilities and talent but also bring over the culture of smaller firms into the rest of their organization via osmosis.

"We're now going to see the same thing with sustainability," says Dondos. "It's not the traditional way you'd expect these companies to acquire. But if you can draw the talent and the approach from one pivotal acquisition, you can reconfigure your whole offering. That can deliver a great deal of value across an organization."



If you can draw the talent and the approach from one pivotal acquisition, you can reconfigure your whole offering. That can deliver a great deal of value across an organization"

Looking forward to 2022

Despite the acceleration of interest in the ESG space, it's clear that while sellers are starting to respond to growing buyer appetites, we are nowhere near a critical mass yet.

"The conversations around sustainability are growing, whether in terms of green energy, net Zero, or more sustainable operational models," says Dondos. "The Big Four are already making moves, with both PWC and Deloitte making billion-dollar investments into hiring and acquiring consultants to develop their practices. It's early days, but it's clear we're at the beginning of something big here."

Such action will also heighten the need for greater transparency and access to data among organizations - chiming with broader platform and digital trends throughout the Knowledge Economy.

"It's likely we'll see a push for greater disclosure and transparency efforts in the new year," says Alex Monck, Director at Equiteq, Australia and New Zealand. "Measuring the impact of sustainability efforts is a real challenge for organizations. In the coming years, data analytics solutions will play a growing role in ensuring businesses are getting results from their ESG projects."

Taking advantage of this trend in 2022

For buyers, now is the time to start exploring opportunities in the sustainability space. With many firms no bigger than boutiques, the prospect of acquisition or investment will likely appeal as they seek to scale up operations and increase their impact.

"With skills in short supply, this is a hot space for any buyer looking to develop their own internal sustainability practice, or to add a

ILLUSTRATIVE DEALS

KKR acquires
Environmental resources
management

KKR
ERM

Environmental Resources
Management acquires The
Renewables Consulting
Group

ERM

Renewables
Consulting
Group

Blackstone acquires
Sphera Solutions

Blackstone

sphera™

The ERM Group acquires
Element Energy

ERM

elementenergy

sustainability component to their service offering," says Masson. "Those that reach a certain size will be very attractive, so we will likely see a lot of consolidation in the coming year and beyond."

For sellers, this may mean developing or amending a service offering to better emphasize how they can help clients become more aligned to ESG themes.

"Going forward, we can expect strategic and financial buyers to quickly clarify their thinking around ESG," says Monck. "Sellers need to be

fully prepared to explain what they are doing and how this can align with an acquirer's ESG-related goals and intent."

The benefits of such investment are clear. Positive impacts on operations, outcomes, and culture furnish an obvious narrative for Strategics, while the growth potential of any asset that benefits both the environment and society should pique the interest of financial investors. The ESG trend may still be in the early stages of adoption, but this should make the available opportunities that much more attractive for any buyer. ○

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