Velocity Global®

February 2021

Cross-Border **M&A Monitor:** Tech Sector

An in-depth review of the key motivations and actions of dealmakers across the IT industry worldwide.

Data provided by PitchBook

Contents

Foreword

Throughout 2020, few sectors accelerated growth like information technology (IT). While the COVID-19 pandemic hindered mergers and acquisitions (M&A) in some sectors, it triggered activity in others. As virtual meeting rooms, digital health consultations, and e-commerce exploded, digitization became an imperative rather than a long-term initiative for companies across the globe. This digitization movement incentivized dealmakers to close deals in progress more swiftly to capitalize upon new opportunities. It also encouraged corporate development teams to look ahead to what capabilities, products, and services they need to acquire or develop.

In 2020, incumbent companies in key tech segments, such as cloud computing or enterprise software, pursued M&A to maintain their commanding market positions or tried to capitalize on surges in demand by investing in areas where the pandemic may have had a permanent effect. Some incumbents in industries such as digital infrastructure engaged in opportunistic dealmaking as their bargaining positions grew stronger. Others in telecommunications completed significant mergers to realize common goals and consolidate market share and offerings. All in all, market surveys reveal significant bullish enthusiasm for dealmaking, whether realizing postponed transactions or engaging in newfound opportunities, and the data supports these findings, showing little slowdown in the pace of global IT M&A.

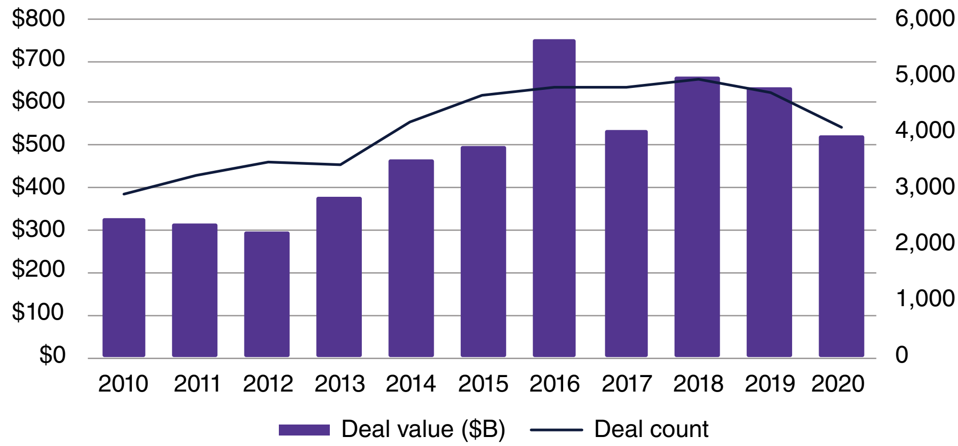
Despite common logistical hurdles and the general uncertainty induced by the pandemic, companies sustained a bullish pace of cross-border M&A as well, with total aggregate value in 2020 matching the level hit in 2019. However, not all types of cross-border expansion and exposure were equally popular; tech carve-outs diminished significantly in volume. This report unpacks the multiple factors at play behind these trends.

Setting the scene: Macro market trends

The five years prior to 2020 were a golden era of tech deals. Global M&A neared 5,000 transactions on an annual basis, while aggregate deal value eclipsed $600 billion in three of those five years. Total value within that timeframe neared a staggering $3.1 trillion. Analyzed through a macro lens, this record-breaking period represented the pervasion of e-commerce across the consumer space, the expansion of enterprise software across B2B, the transition to the cloud, and high-growth advances in IT-specific segments such as cybersecurity. The dealmaking cycle had hardly slowed by the time the unique disruption of the COVID-19 pandemic stormed across the world in early 2020. Q2 registered one of the sharpest declines on record in M&A volume as everyone grappled with the pandemic. However, it took just that one quarter for dealmakers to adapt and pick up the pace of tech M&A in H2.

2020 returns to pre-boom levels

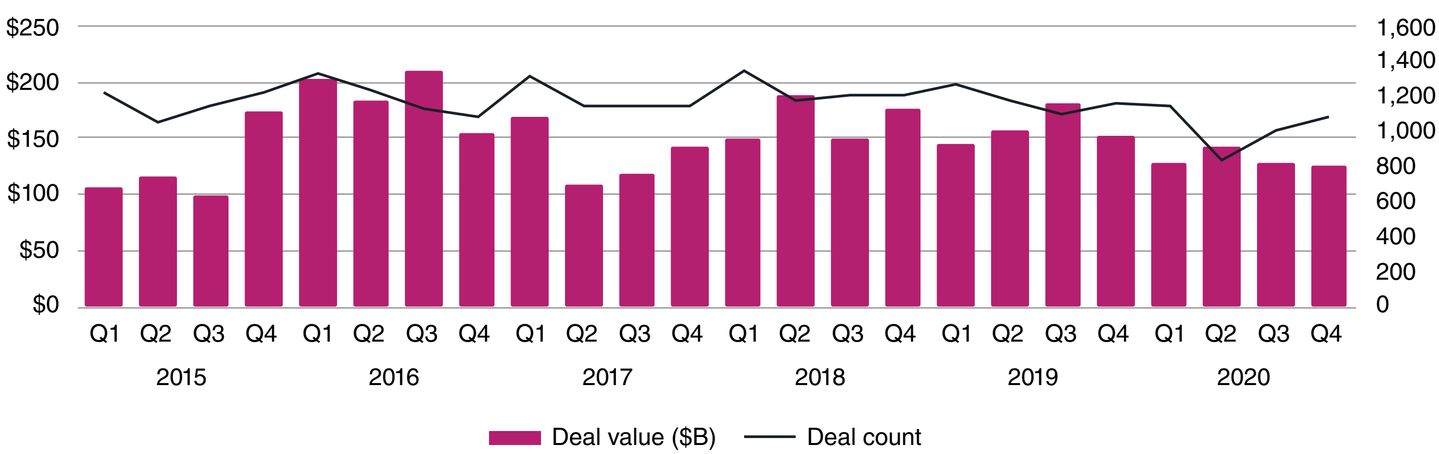
IT M&A activity



Source: PitchBook | Geography: Global

After initial dip, a rebound in M&A volume

IT M&A activity



Source: PitchBook | Geography: Global

The key drivers behind strong M&A

A myriad of factors contributed to the record half-decade of growth and the sheer resilience of tech M&A worldwide. This section summarizes the core drivers pushing this sector forward.

Companies pay up in equity for the right deals, keeping multiples robust

While several developed economies experienced sluggish rates of growth for much of the 2010s, many companies grew inorganically through M&A. Some consolidated with direct competitors to expand market share, while others purchased companies to acquire new capabilities rather than engage in more expensive and time-consuming internal R&D and expansion. Moreover, with one of the greatest bull markets on record and accommodative monetary conditions, M&A was an attractive option from a fiscal standpoint for many tech companies, as they relied on booming share prices and low interest rates.

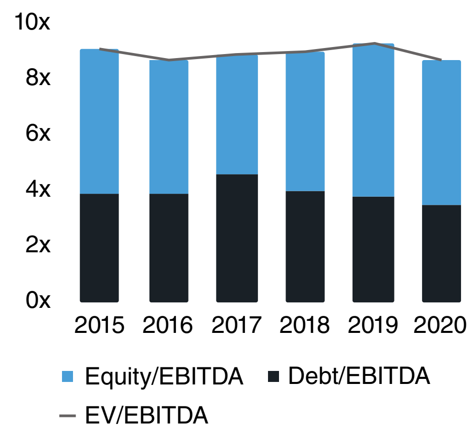
Consolidation and competition are fiercest in software, IT services, and telecommunications

Software closed more deals and generated more deal value than any other subsector. However, both IT services and telecommunications saw significant spikes in deal value in the past couple years, a telltale sign that the largest businesses in the space are merging in blockbuster deals to achieve synergies. At the same time, software giants sought to preclude competition or acquire talent, or both, through acquisition of venture-backed startups at a steady clip.

Financial acquirers push into IT, broadening the base of buyers

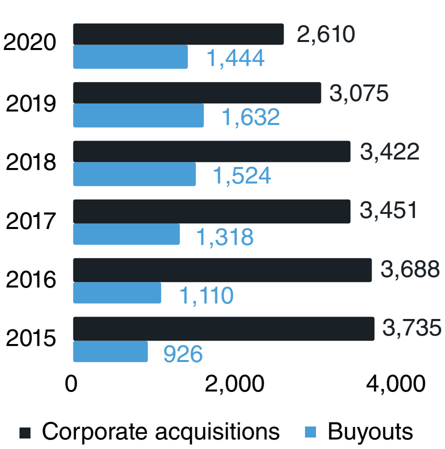
After the first and major movers in the space grew into behemoths, more PE firms pushed into technology, especially software. Armed with over a trillion dollars in dry powder by the end of 2020, these buyers represented a record share of overall M&A volume, helping bolster overall volume. In addition, non-tech businesses acquired brand new digital capabilities as part of their expansion strategies.

Median IT M&A multiples



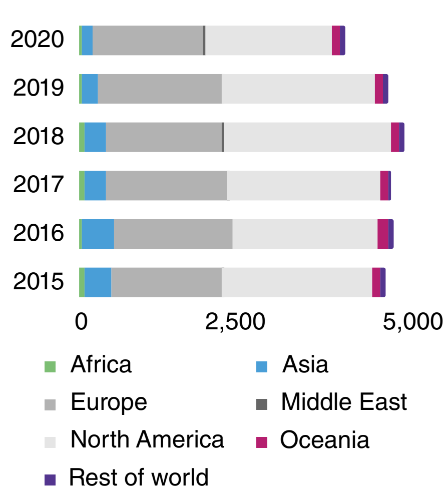
Source: PitchBook | Geography: Global

IT M&A (#) by type



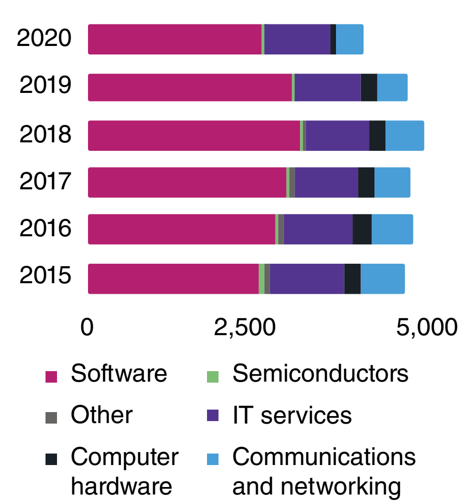
Source: PitchBook | Geography: Global

IT M&A (#) by region



Source: PitchBook | Geography: Global

IT M&A (#) by sector



Source: PitchBook | Geography: Global

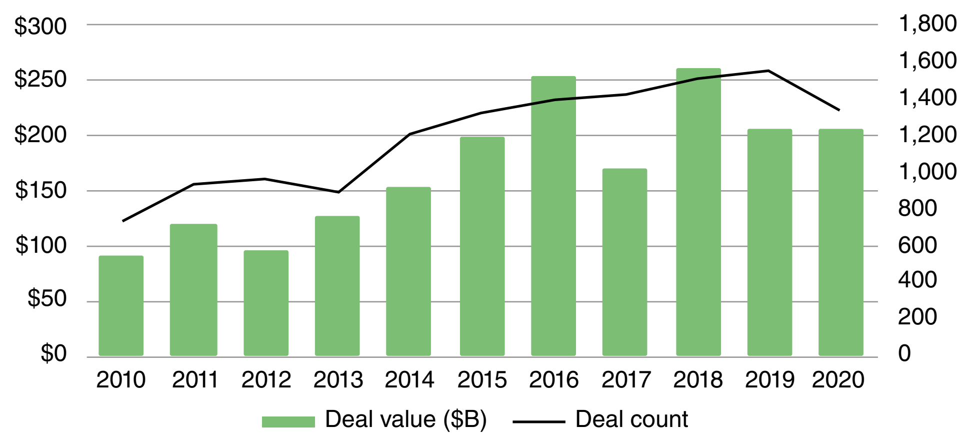
Cross-border expansion remains integral to growth plans

Cross-border tech M&A fared well in 2020, as it remains integral to company growth plans. In 2019, 1,551 cross-border tech deals closed globally, marking a new record, but deal count declined to 1,326 in 2020 for nearly the same approximate deal value. In combination, these figures suggest that aside from a temporary pullback in Q2, COVID-19's impact on the market did not dissuade dealmakers from paying up for transactions.

Europe remained the most resilient region in terms of cross-border IT M&A. Deals occurred across a diverse array of tech subsegments. Examples include Liberty Global's CHF 6.8 billion purchase of triple-play telecom Sunrise Communications in November and Capgemini's acquisition of engineering consulting provider Altran Technologies for €3.7 billion in spring 2020. Cross-border IT M&A activity remains at a high level in this region primarily because of cyclical consolidation in subsectors such as enterprise software and telecommunications. M&A also remains a more attractive access point to a given regional market across the continent.

Aggregate cross-border IT M&A value held steady even as volume dipped

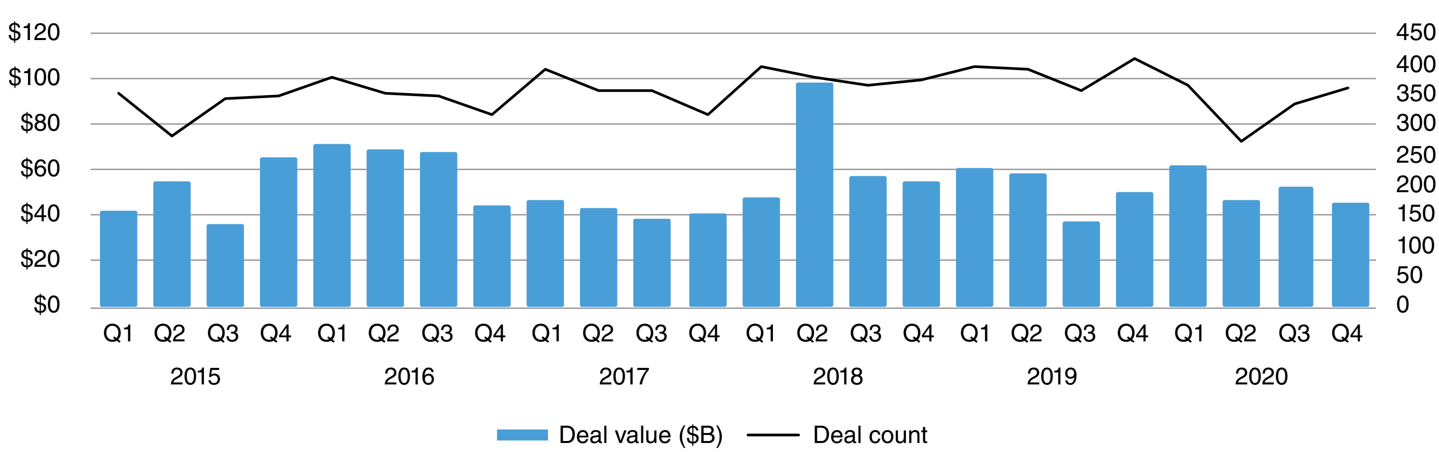
Cross-border IT M&A activity



Source: PitchBook | Geography: Global

After initial plunge in Q2, cross-border dealmaking resumed

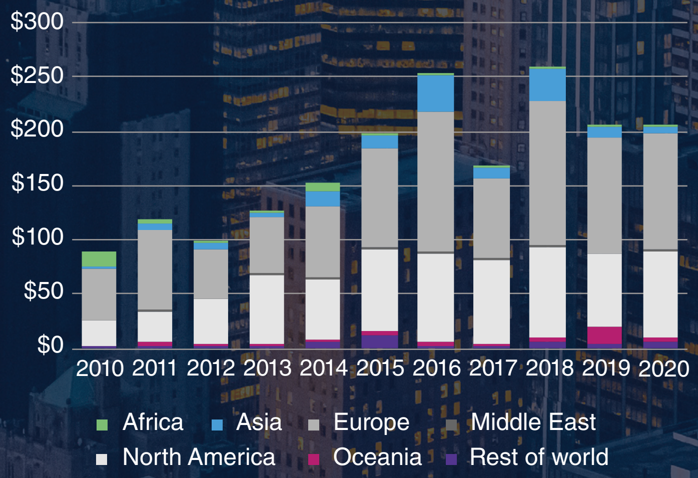
Cross-border IT M&A activity



Source: PitchBook | Geography: Global

Europe eclipses $100B+ in both 2019 and 2020

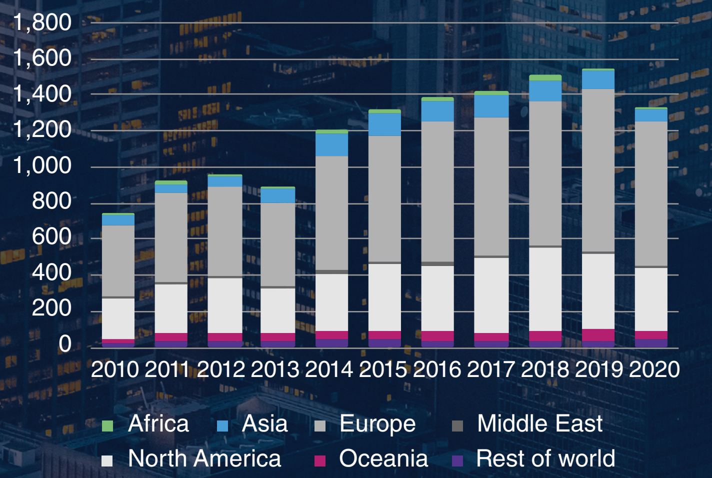
Cross-border IT M&A ($B) by region



Source: PitchBook | Geography: Global

Europe dominates cross-border deal volume

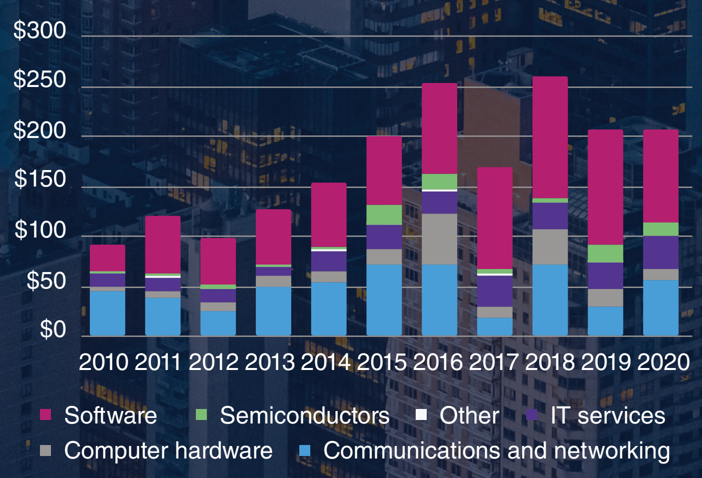
Cross-border IT M&A (#) by region



Source: PitchBook | Geography: Global

IT services and telecommunications see most frequent spikes in deal value

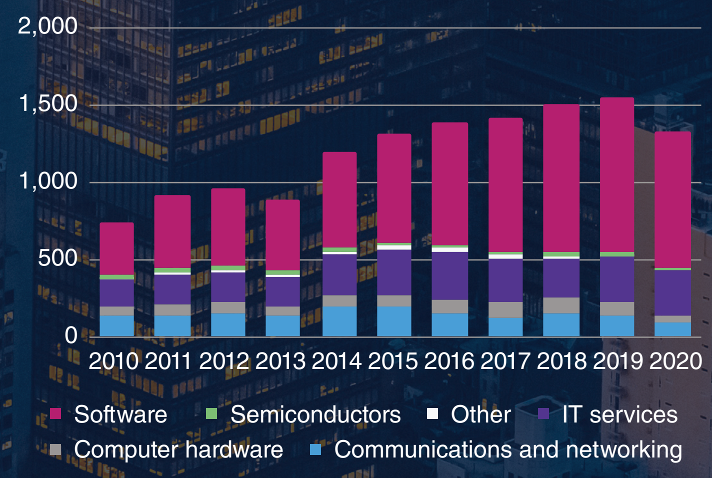
Cross-border IT M&A ($B) by sector



Source: PitchBook | Geography: Global

Volume stays concentrated among three major segments

Cross-border IT M&A (#) by sector



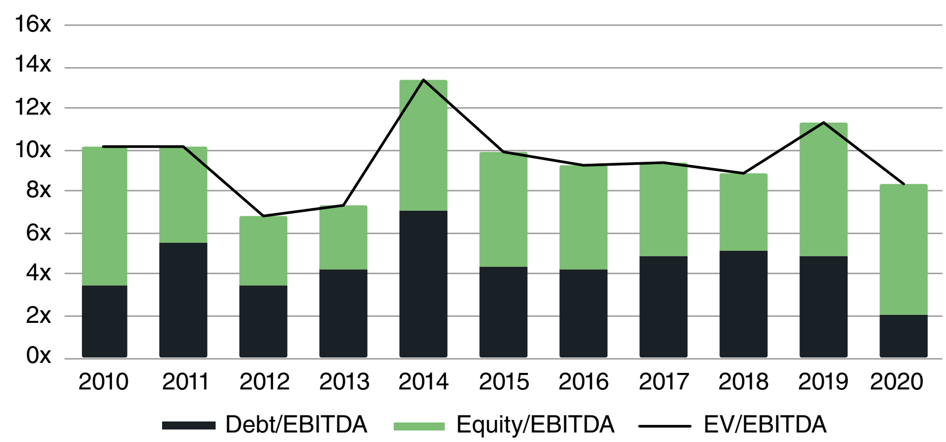
Source: PitchBook | Geography: Global

Hurdles remain significant, especially in a pandemic era

Even prior to COVID-19, prospective cross-border buyers and sellers faced significant challenges. From a personnel perspective, immigration and recruiting to ensure talent remains intact or can grow to the level needed are logistically and operationally complex. Non-domestic regulations, especially in an era marked with heightened geopolitical tensions or outright trade disputes, thwart non-domestic direct investment and derail deals. Even post-merger integration simply takes longer because of remote communications. Due to increased caution, equity portions in M&A multiples surged in 2020, while the deepest-pocketed buyers—PE firms—accounted for a record share of cross-border M&A volume. Dealmakers also targeted mature, stable businesses, acquiring more late-stage, venture-backed businesses than ever before. In short, M&A went forward but primarily for safer prospects.

After spike in 2019, multiples subside as debt portions roughly halve in sign of caution

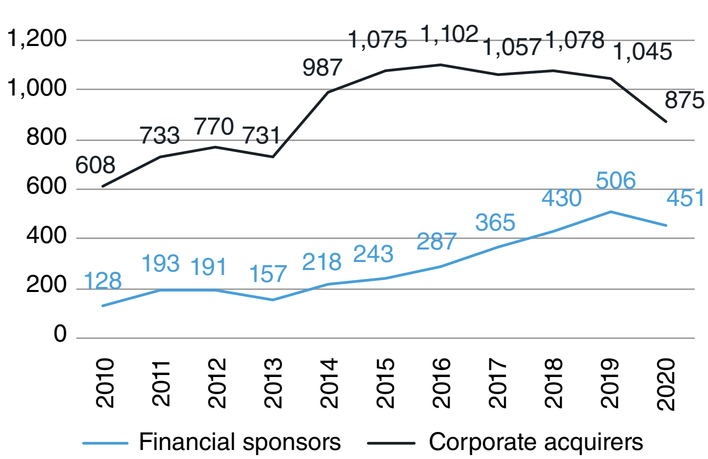
Median cross-border IT M&A multiples



Source: PitchBook | Geography: Global

Resilient PE hits record share of M&A volume

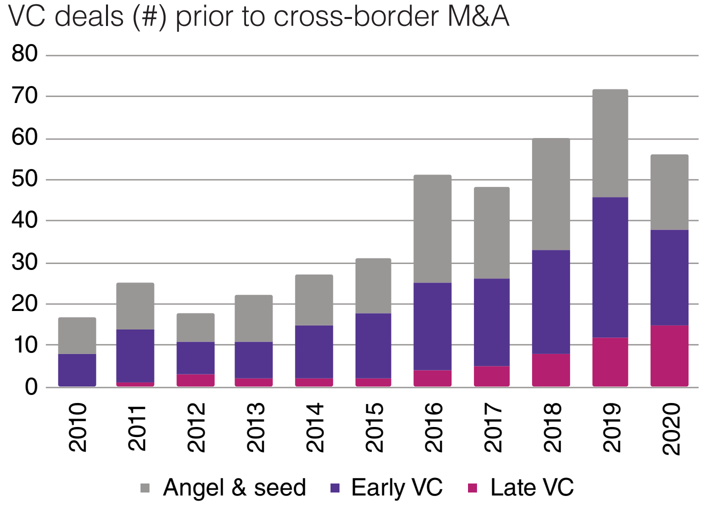
Cross-border IT M&A (#) by buyer type



Source: PitchBook | Geography: Global

Venture-backed targets increasingly rake in late-stage capital prior to cross-border M&A

VC deals (#) prior to cross-border M&A



Source: PitchBook | Geography: Global

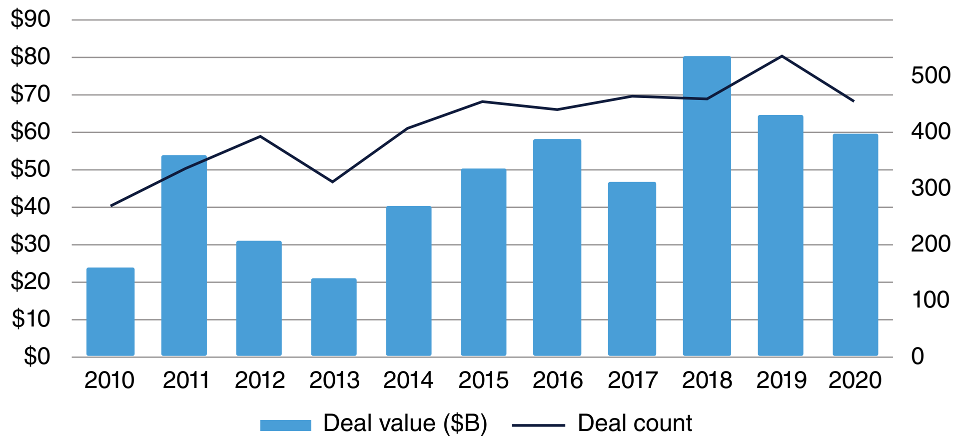
But the rewards outweigh the costs

However arduous the means, the pandemic's resultant policies that led to a widescale remote-work experiment put cross-border dealmaking in a better perspective. In sectors where remote work is possible, many businesses and teams realized how effectively work can be done with digital processes and communication, which made due diligence less daunting. After a steep plunge in the first half of the year, cross-border deal activity rebounded to the elevated levels of previous years. In addition, major U.S. tech giants remained a key bolstering presence in global dealmaking, closing on a pre-2019 level of deals despite the pandemic.

Cross-border transaction activity saw gains from financial buyers, as buyouts accounted for the largest proportion of tech M&A ever, a result of the macro drivers that boosted overall tech M&A. Ongoing international political disputes also encouraged more regionally-focused dealmaking, with the Asia-Pacific region poised for a comeback. The globalization of the venture boom throughout the 2010s also enabled the emergence of multiple cohorts of more mature tech businesses across many regions. In turn, new pools of prospective targets with higher median revenues formed for major acquirers with the means and savvy to pull off cross-border M&A across enterprise security, cloud workflows, and more. As a result, however, deal sizes also climbed.

Aggregate M&A value held steady even as volume dipped

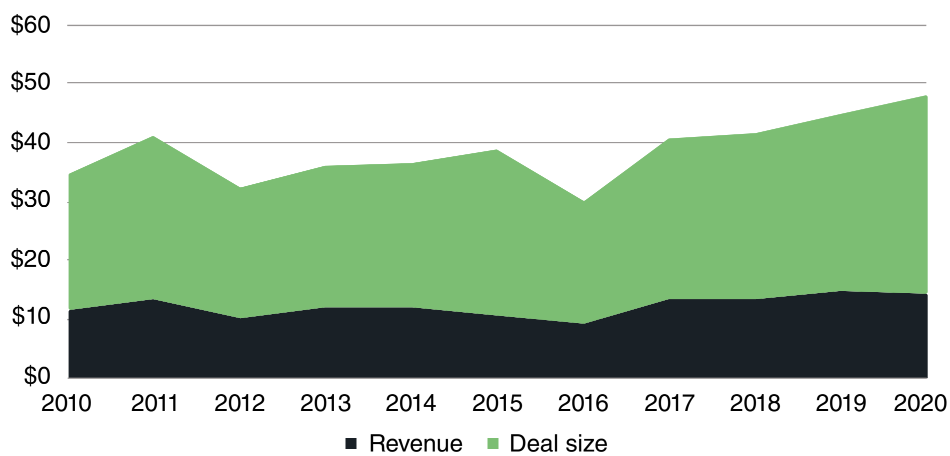
Cross-border IT M&A with U.S.-headquartered acquirers only



Source: PitchBook | Geography: Global

2020 sees surge in average revenues and deal sizes

Median revenues and deal sizes ($M) for cross-border IT M&A



Source: PitchBook | Geography: Global

Cross-border carve-outs increase in complexity—not only due to COVID-19

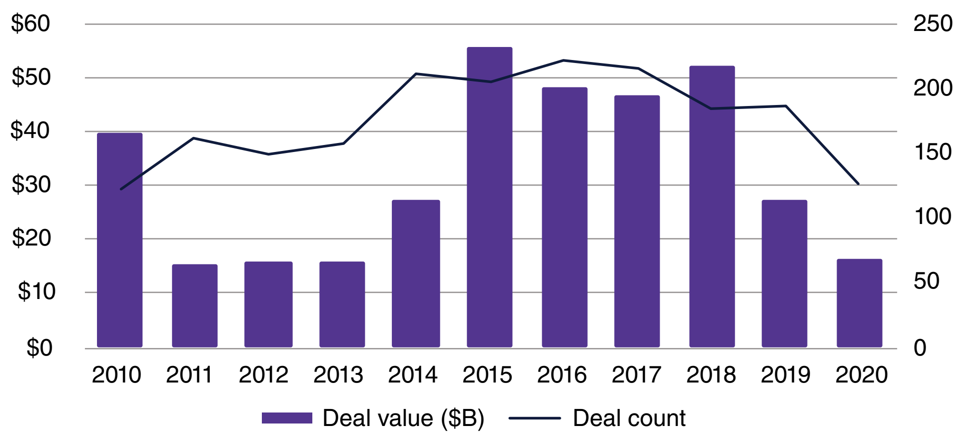
2020 observed a significant decline in cross-border carve-out M&A volume to just under 67% of 2019's tally, which was lofty considering a substantial downturn in aggregate value that year. However, quarterly figures reveal a resurgence in volume after the Q2 dip. Given the complexities inherent in carve-outs, the additional uncertainty wrought by the COVID-19 pandemic discouraged carve-outs throughout the year.

This report's analysis also reviewed cross-border M&A sized $25 million or less to determine if dealmakers really eschewed carve-outs because of those complexities or if they just decided that cross-border purchases below that $25 million threshold weren't worthwhile. The aggregate value of deals in that smaller bucket was fairly resilient, which suggests it was carve-outs' specific characteristics that dissuaded dealmakers rather than the size of the deal.

Given their popularity in recent years, though, it is important to note that carve-outs in and of themselves did not suddenly ramp up in difficulty. Carve-outs are more complicated than outright, wholesale acquisitions, given the need to have proper integration plans in place, conduct both operational and financial due diligence, and assess isolated financials and overall technology risks in terms of licensing, transition service agreements (TSAs), and more. One notable trend in the data is that the proportion of software carve-outs nearly dropped by half between 2019 and 2020, with aggregate value falling by roughly

Carve-outs plummet to nearly 67% of 2019 volume

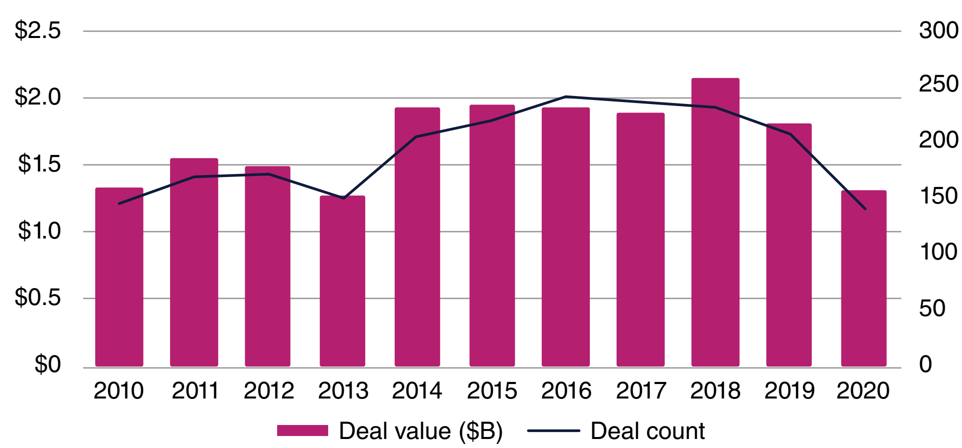
Cross-border IT carve-out activity



Source: PitchBook | Geography: Global

Despite pandemic, smaller cross-border IT M&A declines to only 2013 levels

Cross-border IT M&A activity, ≤ $25M

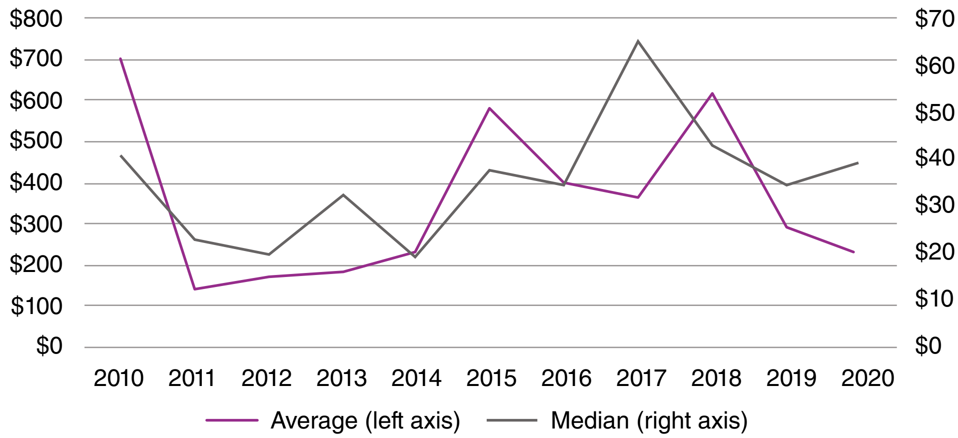


Source: PitchBook | Geography: Global

two-thirds. This signals what primarily drove the decline in average cross-border carve-out sizes. Given the geopolitical landscape and the trend toward pricier acquisitions, intellectual property and rights agreements that necessitated daunting TSAs made it more difficult to justify spending significant sums on other companies' business units or divisions, particularly in software, rather than on outright M&A or in-house development. In addition, although they bolstered overall cross-border carve-outs in tech over the past four years, PE firms did not spend as much as they might have due to the level of deal multiples, overall. That said, they maintained at least roughly the same level of activity as they did in 2018.

Median hits third-highest tally of past decade as average slides

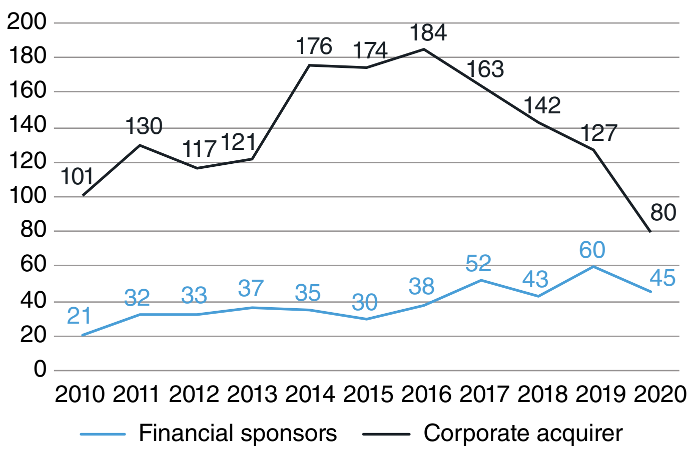
Average and median cross-border IT carve-out sizes ($M)



Source: PitchBook | Geography: Global

PE firms bolster carve-out volume

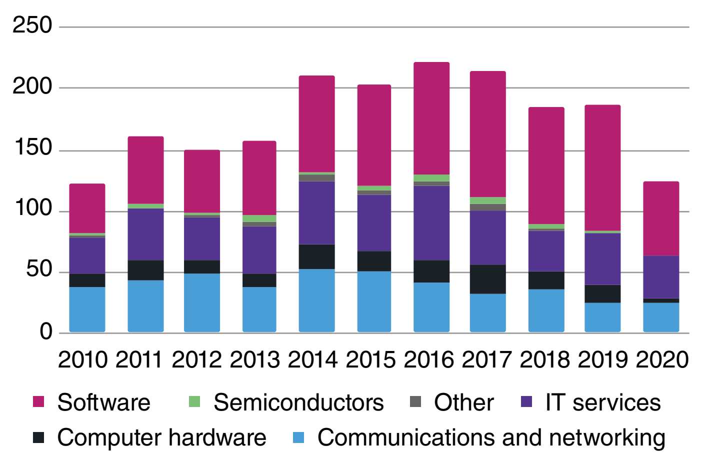
Cross-border IT carve-outs (#) by buyer type



Source: PitchBook | Geography: Global

Software sees largest proportionate decline in activity

Cross-border IT carve-outs (#) by sector



Source: PitchBook | Geography: Global

Conclusion

The varied array of uncertainties that kicked off 2020—Brexit, protectionism, regional conflicts—all paled in comparison to the juggernaut of the COVID-19 pandemic. However, judging by the macro trends in data, dealmakers across the IT space eventually took the pandemic in stride as much as they did those other concerning trends. Incentives to engage in mergers, buy out regional rivals to shore up market share across national boundaries, and acquire new capabilities outweighed all of the logistical and operational hurdles that culminated from those varied challenges.

Looking ahead to 2021, the resurgence in dealmaking throughout the back half of 2020 persists, but not quite at such a frenetic pace. The full economic ramifications of the pandemic remain unknown, and the acceleration in key tech subsectors prompts M&A activity. Regardless of recent fortune, some of the prominent winners of the shift to remote work and digitization in 2020 will have to contend with fierce competition from established tech giants or far less rapid growth rates. Prospective dealmakers, both buyers and sellers, must take these factors into account, as the COVID-19 vaccine rolls out and businesses return to normal in the back half of 2021. Key questions remain. How permanent, and to what degree, are some of the changes that businesses across multiple industries have absorbed? Will regulatory oversight intensify, as well as protectionism across borders that further complicates cross-border M&A in particular, on top of doing business?

While answers to these questions will play out in the year ahead, partnering with an experienced International PEO provider, like Velocity Global, helps dealmakers expedite cross-border transactions and accelerate growth into tech subsectors. This solution allows dealmakers to retain employees in carve-out scenarios, protect intellectual property, and compete on deals in any global market, regardless of existing geographic footprints. International PEO streamlines complex cross-border carve-outs by removing the TSA process and provides a smooth transition for newly acquired global teams.

By and large, heading into 2021, dealmakers are accentuating the positive, eager to once again propel dealmaking to expand and improve their businesses.

Methodology

Source: All the data in this report is sourced from PitchBook. Only completed transactions were included.

Geography: The geographic scope of the data, unless otherwise noted, is global. PitchBook's standard geographic regions were used to break out M&A activity by region.

Extrapolation & sample sizes: M&A aggregate values are extrapolated due to sample sizes. All data points can be presumed to be based on samples of no smaller than n = 20; otherwise, it shall be noted.

Sector: All data in this report is within the Information Technology sector as defined by PitchBook, unless otherwise noted.

Cross-border: Cross-border M&A was defined as when two companies engaged in an M&A event have headquarters in differing countries. Cross-border carve-outs were defined similarly.

Carve-outs: The following list of transaction types were used to define carve-outs: 1) corporate divestiture both financial and strategic; 2) asset acquisition; 3) asset divestiture.

About Velocity Global

Velocity Global helps companies grow globally. Founded in 2014, Velocity Global's clients rely on its expertise and global infrastructure in 185 countries to hire compliantly around the world, increase revenue, scale efficiently, and access global talent. Named a "Leader" in Global Employer of Record services by prominent analyst firm NelsonHall, Velocity Global is a strategic partner to its clients with comprehensive services led by its core offering of International PEO as well as Immigration, Entity Setup and Support, Global Talent Acquisition, and Consulting. Velocity Global is headquartered in Denver, Colorado, with regional headquarters in Amsterdam and Singapore, and local employees in 14 countries.

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