2011 Mid-Year Technology M&A Review

PEACHTREE CAPITAL ADVISORS

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Peachtree Capital Advisors, Inc. is a New York-based investment bank providing M&A advisory services to growth and middle market technology, digital media, and green technology companies both in the U.S. and abroad. With 15 years of experience, Managing Director and founder John Doyle has closed and structured over twenty-five deals and possesses a strong knowledgebase of financial and strategic buyers in these sectors. If you are interested in learning more about valuation, positioning, preparation, or the merger and acquisition process, please visit www.peachtreecapitaladvisors.com or contact John Doyle at 212-570-1009.

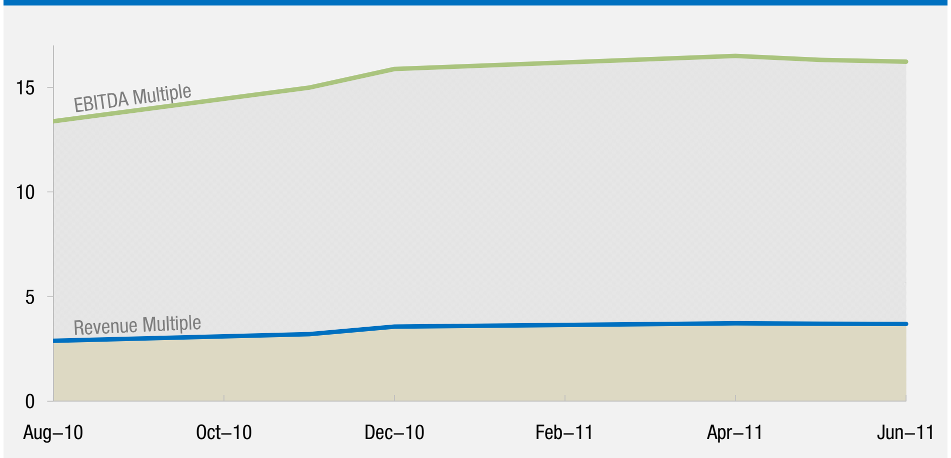
2011 First-Half Technology M&A

Despite a sluggish economy, technology M&A rode its momentum from late 2010 to enjoy a solid first half in 2011. Although valuations in the technology sector did not rise substantially following steady growth in 2010 (see Figure 1), they remained relatively constant throughout the first half of the year, providing necessary stability and support for the M&A marketplace. Large-cap companies, having accumulated a buildup of cash during the recession, emerged as major spenders, pursuing acquisition growth strategies rather than investing in organic growth.

Whereas technology M&A activity was largely driven by increased valuations in 2010, enterprise interest in the cloud and the renewed deployment of capital from private equity firms emerged as major themes in early 2011. Although the "cloud" may be the most overused technology buzz word in recent memory, it has nevertheless fundamentally changed the landscape of information technology by centralizing everything in one place.

Due to the increased demand among enterprises for products that utilize the cloud, IT service companies offering cloud computing services were attractive acquisition targets in the first half of 2011. For example, Verizon acquired the cloud infrastructure-as-a-service provider Terremark Worldwide in January and CenturyLink acquired the cloud-computing IT services company Savvis in April. This cloud computing trend in technology will likely continue in the second half of the year as large-cap corporations continue their pursuit of cloud computing capabilities.

Figure 1: Technology Sector Valuations, August 2010 – June 2011



The first half of 2011 also witnessed increased M&A activity from the private equity sector, which had been very quiet for the duration of the recession. Many private equity firms returned from the sidelines in 2010 to jumpstart their deal flow, and private equity deal volume rose again in the first half of 2011 on the strength of several large April acquisitions.

In the same month, Providence Equity Partners took IT consulting firm SRA International private for $1.9 billion, while Infor, a subsidiary of Golden Gate Capital, and Apax Partners both made enterprise resource planning (ERP) acquisitions. Infor acquired Lawson Software for $1.8 billion and Apax Partners spent nearly $2 billion to purchase Epicor Software and Activant Solutions in separate transactions. As economic conditions improve and credit becomes more readily available, private equity firms should remain highly visible in technology M&A. ■

Enterprise Software

Enterprise software M&A activity in the first half of 2011 was headlined by high-profile acquisitions in the highly competitive ERP sector (see Figure 2). In March, Golden Gate Capital and Infor announced an unsolicited bid to acquire Lawson Software, which was followed several weeks later by Apax Partners' separate acquisitions of Epicor and Activant Solutions. These acquisitions signaled a trend of consolidation in the once-fragmented ERP sector.

Figure 2: Enterprise Software Valuations and Acquisition Multiples ($M)

Public	Company	Market Cap	Enterprise Value	REV Mutiple	EBITDA Multiple
	CA Technologies	11,560	9,970	2.3x	6.5x
	Compuware	2,130	1,950	2.1x	9.7x
	EMC	56,690	54,550	3.1x	14.1x
	JDA Software	1,310	1,357	2.1x	8.4x
	Microsoft	219,250	183,690	2.7x	6.1x
	Oracle	166,690	153,760	4.3x	9.9x
	Quest Software	2,040	1,716	2.2x	11.7x
				2.7x	9.5x
Acquired	**Company**	**Transaction Value**	**Enterprise Value**	**REV Mutiple**	**EBITDA Multiple**
	Epicor Software	976	1,117	2.5x	20.5x
	Lawson Software	1,839	1,781	2.4x	15.4x
	Telvent GIT	1,598	2,034	2.0x	12.4x
	Vital Images	273	133	2.2x	23.5x
				2.3x	17.9x

While the ERP market has long been dominated by Oracle and SAP, competition has recently intensified. With the boundaries of ERP continually expanding, the top vendors have adopted a strategy of assembling comprehensive ERP suites that can be offered to customers as a single solution. Infor and Apax were able to accomplish this goal through their acquisitions of Lawson, Epicor, and Activant—all three were top ten ERP vendors whose technology will now be integrated into a more complete ERP offering.

Infor (Golden Gate Capital) Acquires Lawson Software

On April 26, Infor Global Solutions, a subsidiary of private equity firm Golden Gate Capital, announced the acquisition of Lawson Software for $1.8 billion, six weeks after making an initial bid. Infor paid $11.25 per share, which was a 14% premium on Lawson's closing share price on March 7—the last day of trading prior to news of the potential takeover and four days before the actual unsolicited offer, which Lawson ultimately accepted.

The acquisition of Lawson continues Golden Gate Capital's recent involvement with enterprise software. In the past five years, Golden Gate Capital has invested in or acquired more than forty software companies with combined revenues of $4 billion, many of which were acquired for Infor, Golden Gate's largest software portfolio company. In a market where profitability is driven by size and economies of scale, Infor has become a major software player through this acquisition roll-up strategy. The Lawson acquisition increases Infor's customer base to 75,000 and revenue to approximately $3 billion.

For Infor, an ERP provider whose product line also extends into other areas of enterprise software, the Lawson acquisition adds breadth and reach to its ERP lineup. According to Infor CEO Charles Phillips, Lawson's enterprise financials and human resources products will integrate with Infor's manufacturing, supply chain, workforce, and asset management products to comprise a complete ERP suite. Lawson also provides Infor with additional clout in the healthcare, manufacturing, distribution, fashion, food and beverage, and public sector verticals.

From an M&A perspective, the 2.4x revenue multiple paid for Lawson seems relatively low. However, Lawson mainly serves small to mid-sized customers, where margins are lower than with larger, higher-end clients. Additionally, Lawson's growth has sputtered since acquiring Intentia in 2006, and its revenue has actually fallen from a peak of $852 million in 2008 to $736 million in 2010.

Apax Partners Acquires Epicor Software and Activant Solutions

On April 4, private equity firm Apax Partners acquired enterprise software company Epicor Software for $976 million. It paid $12.50 a share, which was an 11.2% premium over Epicor's closing price on April 1, the last trading day prior to the announcement. On the same day, Apax separately acquired Activant Solutions, a privately-held provider of business management software solutions, and announced its intention to merge the two companies to create a global provider of enterprise applications with over 30,000 customers and $825 million in annual revenues. The new company will operate under the name Epicor Software Corporation.

By acquiring Epicor and Activant, Apax

Enterprise Software

Partners establishes a sizable presence in the ERP market where size is necessary to compete. Many software companies view the billion-dollar revenue threshold as a significant barrier to advantages in economies of scale, and the newly-combined entity approaches this figure with $825 million in combined revenue. While Epicor and Activant were both midmarket ERP vendors, the two combined attain added scale to potentially compete with market leaders Oracle and SAP for higher-end clients. Additionally, the two companies enjoyed many synergies in their vertical focus, and the merger further strengthens their presence in the manufacturing, retail, and distribution industries.

The $976 million paid for Epicor translates to a 2.5x revenue multiple, which almost mirrors the valuation paid in the Lawson acquisition. Like Lawson, it has struggled to grow in recent years, with revenue declining in two of the past four fiscal years and growing less than 3% overall since 2007. Both the merger with Activant and the financial backing of Apax Partners, however, will enable Epicor to grow more aggressively following the acquisition.

Toshiba Medical Systems Acquires Vital Images

On April 27, Toshiba Medical Systems (TMSC), a subsidiary of Toshiba Corporation, acquired Vital Images for $273 million. It paid $18.75 per share, which was a 31.5% premium over the closing price of $14.26 on April 26. Vital Images provides advanced visualization and analysis software for the healthcare industry, and TMSC hopes to significantly strengthen its Imaging Solutions division by acquiring the company.

Following a decade-long partnership between the two companies, this transaction was a logical step for Toshiba. TMSC has for many years been Vital Images' largest customer and last year supplied more than 50% of the company's $59.7 million in revenue. The acquisition allows TMSC to bolster its product offerings by integrating Vital Images' technology into its product line and realize economies of scale by combing the two operations.

Although Vital Images' transaction value was a lofty 4.6x revenue, the company was also cash-rich with no debt on its balance sheet. After adjusting for enterprise value, the deal was valued at 2.2x revenue, which is more in line with the valuation for a company that has seen its revenue steadily decline more than 15% since 2006. ■

Internet

While overall technology valuations remained relatively flat in the first half of 2011, the Internet sector saw a substantial uptick during this period, with revenue multiples rising from 3.5x to 4.5x. The rise in valuations set the tone for a series of substantial acquisitions, including four publicly-traded companies being acquired for an average of 4.3x revenue (see Figure 3). In particular, real estate data firm LoopNet was acquired by its rival, CoStar Group, for 9.5x revenue—more than double the average valuation in the Internet sector.

Acquisitions in the Internet sector primarily fell into two buckets: e-commerce buyers acquiring to diversify their customer base and traditional buyers acquiring to bolster their online presence.

Figure 3: Internet Valuations and Acquisition Multiples ($M)

Public	Company	Market Cap	Enterprise Value	REV Mutiple	EBITDA Multiple
	Digital River	1,280	911	2.5x	19.6x
	Google	163,180	131,600	4.2x	10.8x
	Keynote Systems, Inc.	353	267	3.0x	20.7x
	LivePerson	745	678	5.9x	28.6x
	Rightnow Technologies	1,070	995	5.1x	46.8x
	Verisign	5,640	4,274	6.1x	13.1x
	Salesforce.com	19,950	19,714	11.1x	142.2x
				4.5x	23.3x
Acquired	**Company**	**Transaction Value**	**Enterprise Value**	**REV Mutiple**	**EBITDA Multiple**
	GSI Commerce	2,400	2,190	1.6x	33.0x
	Drugstore.com	429	410	0.9x	20.5x
	LoopNet.com	860	763	9.5x	35.4x
	MediaMind Technologies	517	416	5.0x	27.1x
				4.3x	29.0x

Both CoStar Group and eBay, which acquired GSI Commerce, were both e-commerce companies that made acquisitions to reach new customers—CoStar Group, to extend beyond its base of commercial customers to reach individuals, and eBay, to propel itself beyond small merchants and toward large retailers. Meanwhile, the acquisitions of Drugstore.com by Walgreens and MediaMind Technologies by DG featured buyers who saw the need to make an online play—Walgreens, to strengthen its weak e-commerce platform, and DG, to integrate digital advertising with its traditional ad serving model.

Walgreens Acquires Drugstore.com

Walgreen Co. acquired Drugstore.com in March for $429 million, or $3.80 per share, in an all-cash deal. The acquisition price represented a 113% premium over the last closing price before the transaction was announced on March 24, 2011.

Although Walgreens is the largest drugstore chain in the United States, it has not invested heavily in developing an e-commerce and mobile commerce presence. The drugstore juggernaut addresses this weakness through the Drugstore.com acquisition, in which it also gains control of Beauty.com and SkinStore.com, properties owned and operated by Drugstore.com. The deal also positions Walgreens to challenge e-commerce leader Amazon.com, which operates two chief competitors of Drugstore.com, Soap.com and Diapers.com.

The acquisition marks the successful end to a yearlong pursuit of Drugstore.com by Walgreens. After rejecting two earlier offers, Drugstore.com approved the third proposal offering a hefty price-per-share premium in excess of 100%. With an enterprise value of $410 million, however, Drugstore.com was only valued at 0.9x revenue despite the large premium. Walgreens was able to negotiate this low acquisition price since Drugstore.com was unprofitable during the last fiscal year. Walgreens hopes to expand its e-commerce operations through the acquisition and turn Drugstore.com profitable in the process.

eBay Acquires GSI Commerce

In March, auction giant eBay acquired online services company GSI Commerce for $2.4 billion. The acquisition price of $29.25 per share represented a 51% premium over the last closing price prior to the March 28 transaction announcement. Under the agreement, eBay divested all of GSI's licensed sports merchandise business and 70% of e-commerce sites ShopRunner and Ru La La, calling these assets "not core to its long-term growth strategy." The divested assets were spun off into a holding company equipped with a $467 million loan from eBay and led by GSI Commerce CEO and founder Michael Rubin. Rubin also invested an additional $31 million into the holding company.

The acquisition of GSI Commerce is a strong strategic buy for eBay. In particular, eBay is attempting to transform itself into an e-commerce platform in order to take advantage of the high growth in the e-commerce space. As an online service company focused on creating and operating websites for retailers, GSI Commerce

Internet

has strong relationships with large retailers such as Toys “R” Us and Kenneth Cole. By acquiring GSI, eBay will obtain numerous retail clients and gain the technology necessary for eBay to fill large orders for retailers. As a result, eBay hopes that it will be able to successfully compete with Amazon.com for retail e-commerce business.

This deal is wonderful news for GSI, which received 33x EBITDA in the acquisition. Recently struggling to integrate its sports merchandise arm as well as Ru La La into the company, GSI is content to hand over operations to the well-seasoned eBay management and earn a respectable premium in the process. However, it still remains to be seen whether this acquisition will be successful for eBay given that eBay is somewhat new to the e-commerce platform space and given eBay’s murky acquisition history as evidenced by its unsuccessful acquisition of Skype.

CoStar Group, Inc. Acquires LoopNet, Inc.

In April, real estate information provider CoStar Group acquired its rival LoopNet in a cash and stock transaction worth $860 million. LoopNet shareholders received $16.50 in cash and 0.03702 shares of CoStar stock per share of LoopNet stock, 15% higher than the pre-announcement closing price on April 26.

CoStar is a commercial real estate information firm that provides premium real estate research, marketing, and analytics services. Due to its expensive services, CoStar has lately encountered difficulties in expanding the company’s client base. LoopNet, meanwhile, is a commercial real estate marketplace whose lower-quality, computer-generated data has enabled the company to price more aggressively. Although CoStar and LoopNet posted similar revenue numbers in the past fiscal year, LoopNet achieved higher net income margins despite its lower price points. As a long-time rival and competitor, CoStar decided to acquire LoopNet before it could potentially outgrow CoStar.

Due to LoopNet’s strong financials, CoStar paid a large premium to induce LoopNet to accept the deal. After adjusting for cash and debt, the acquisition price represented a revenue multiple of 9.5 and EBITDA multiple of 35.4—both of which are significantly higher than industry averages. Additionally, the board of LoopNet withheld its support for the acquisition until CoStar consented to offering stock as part of the acquisition. Both companies are optimistic about the future of the new CoStar, but it remains to be seen whether the acquisition will be a success due to substantial differences between the business models of CoStar and LoopNet.

DG Acquires MediaMind Technologies Inc.

Less than a year after MediaMind Technologies’ IPO, DG acquired the company in June for $517 million cash, or $22 per share. This represented a 36% premium over the last closing price prior to the June 16 announcement.

DG is an ad serving company focused on television ad delivery with more than 5,000 ad agencies and advertisers as clients. As advertisers increasingly wish to coordinate ad campaigns across multiple media such as television, print, radio, and the Internet, DG realized that it needed to expand its product offerings outside of traditional media. As a digital ad technology firm, MediaMind presented DG with the opportunity to offer internet ad technology products. The acquisition will assist DG in developing into a full-service ad serving company and also provide expected cost synergies of $15 million.

With 24% revenue growth in the past year and healthy profit margins, MediaMind commanded robust enterprise value multiples of 5x revenue and 27x EBITDA in the acquisition. Although not likely to spur any new M&A trends, DG’s acquisition of MediaMind demonstrates the convergence between traditional and online advertising. It is likely, however, that M&A activity will remain high in the online advertising space over the next few years as traditional advertisers continue to move tier budgets into digital media. ■

IT Services

The IT service sector has witnessed significant M&A activity during the first six months of 2011. This activity is largely the result of the increased popularity of cloud computing among telecommunications companies. Suffering from declining telephone and cable service revenue, American telecommunications companies have been actively searching for new high-growth revenue sources. Many of these companies have come to the conclusion that offering computer resources on the cloud will enable them to compete for large enterprise and government agency contracts given the newfound popularity of cloud computing among enterprises and within the Obama administration.

As a result, the first half of 2011 witnessed the acquisition of numerous IT services companies (see Figure 4) providing cloud infrastructure-as-a-service by telephone companies and cable companies. This trend is likely to continue for the next year as telecommunications companies without cloud computing capabilities look to catch up with their competitors.

Figure 4: IT Services Valuations and Acquisition Multiples ($M)

Public	Company	Market Cap	Enterprise Value	REV Mutiple	EBITDA Multiple
	CIBER, Inc	395	427	0.4x	17.0x
	Cognizant Technology	22,310	20,140	4.0x	19.0x
	MicroStrategy	1,740	1,537	3.2x	30.3x
	Perficient, Inc.	312	293	1.3x	15.2x
	Syntel, Inc.	2,470	2,192	3.9x	16.3x
	Virtusa Corporation	482	388	1.8x	15.0x
	Computer Sciences Corp.	5,880	6,620	0.4x	3.0x
	Unisys	1,110	896	0.2x	2.1x
				2.4x	18.8x

Acquired	Company	Transaction Value	Enterprise Value	REV Mutiple	EBITDA Multiple
	Ness Technologies Inc.	307	342	0.6x	8.8x
	SAVVIS	2,500	3,162	3.2x	12.5x
	NaviSite Inc.	230	277	2.1x	10.8x
	Terremark Worldwide	1,400	1,854	5.8x	24.7x
	SRA International	1,880	1819.398	1.1x	20.2x
				2.6x	15.4x

Verizon Communications Inc. Acquires Terremark Worldwide

In January, Verizon Communications Inc. acquired Terremark Worldwide for $1.4 billion in an all-cash deal. The acquisition price of $19 per share represented a 35% premium over the last closing price prior to the January 27 transaction announcement. After the deal closes, Terremark will operate as a wholly owned subsidiary of Verizon under the Terremark name and Terremark's current management.

Verizon is primarily known for its consumer telephone services. However, it also has numerous enterprise clients. In an attempt to take advantage of the popularity of cloud computing among enterprises, Verizon recently developed an "everything-as-a-service" cloud strategy in which it hopes to provide all of the computer services that enterprises and government agencies need on the cloud. This strategy would allow Verizon to compete with Amazon for future enterprise and government contracts.

Terremark was an attractive target to promote this strategy. Terremark offers VMware-based cloud infrastructure-as-a-service, carrier-neutral colocation, and managed hosting. As a result, Verizon acquired Terremark to enhance its public cloud services as well as to acquire Terremark's numerous government agency clients. It is also not surprising that Terremark was interested in selling. Mired with debt after building numerous datacenters, Terremark was pleased to let a more established company assume its large liabilities.

The acquisition of Terremark has subsequently spurred other acquisitions of IT services companies with cloud-computing expertise by telecommunications giants. Examples include the acquisition of Savvis by CenturyLink and the acquisition of NaviSite, Inc. by Time Warner Cable. Cloud computing is a space with the potential for extremely high growth over the next few years. Verizon's competitors will not allow Verizon to partake in the potentially large revenues in cloud computing unchecked. As a result, this trend is likely to continue over the next year.

Providence Equity Partners Acquires SRA International, Inc.

Providence Equity Partners acquired SRA International, Inc. in April for $1.88 billion, or $31.25 per share. The acquisition price represented a 10.2% premium over the last closing price before the transaction was announced on April 1, 2011, and a 52.8% premium over the unaffected share price at market closing on December 31, 2010. SRA will continue its operations under its current senior management team after the deal closes.

IT Services

In contrast to Terremark, SRA International does not specialize in cloud computing. Rather, it offers a wide range of IT consulting services to government agencies, especially national security agencies. From 2008 through 2010, SRA experienced decreasing EBITDA and net income. As a result of SRA's deteriorating financial situation, it sought out strategic as well as financial buyers. Providence Equity Partners, a private equity firm based in Rhode Island, was a natural choice as SRA's acquirer given the strong connection between the two companies. In particular, Renato DiPentima, who recently served as President and CEO of SRA, was hired by Providence Equity in early 2010 as a senior advisor.

Providence Equity's financial acquisition of SRA should be viewed outside of the recent trend of cloud computing acquisitions in the IT services sector. Although the acquisition does not portend any new sector trend, it does serve as evidence of the rapid return of private equity activity as the global economy recovers from the recent financial crisis.

CenturyLink, Inc. Acquires Savvis, Inc.

In April, CenturyLink, Inc. acquired Savvis, Inc. in a cash and stock transaction with an equity value of $2.5 billion and an enterprise value of $3.2 billion. Savvis shareholders received $30 in cash and $10 of CenturyLink stock per share of Savvis stock, which represented an 11% premium over the last closing price before the transaction was announced on April 27 and a 53% premium over the share price from the beginning of 2011.

Savvis' acquisition is staunchly in line with the M&A trend in IT services established by Verizon's acquisition of Terremark. CenturyLink is a telephone company experiencing stagnating telephone service revenue. Similar to Verizon, CenturyLink hopes to gain new enterprise and government contracts by offering cloud-computing services. Its acquisition of Savvis allows CenturyLink to do so. Savvis offers managed hosting, cloud computing, and colocation services to both enterprises and government agencies. With its acquisition of Savvis, CenturyLink will operate 48 datacenters in North America, Europe, and Asia and have the ability to offer comprehensive cloud-computing services to its customers.

Gartner projects that worldwide cloud services revenue will more than double by 2014. As the sector continues to expand rapidly, it is likely that telephone companies will continue to acquire IT services companies focused on cloud infrastructure. This trend may even extend to all telecommunications companies as evidenced by Time Warner Cable's announced acquisition of managed cloud service provider NaviSite in February. ■