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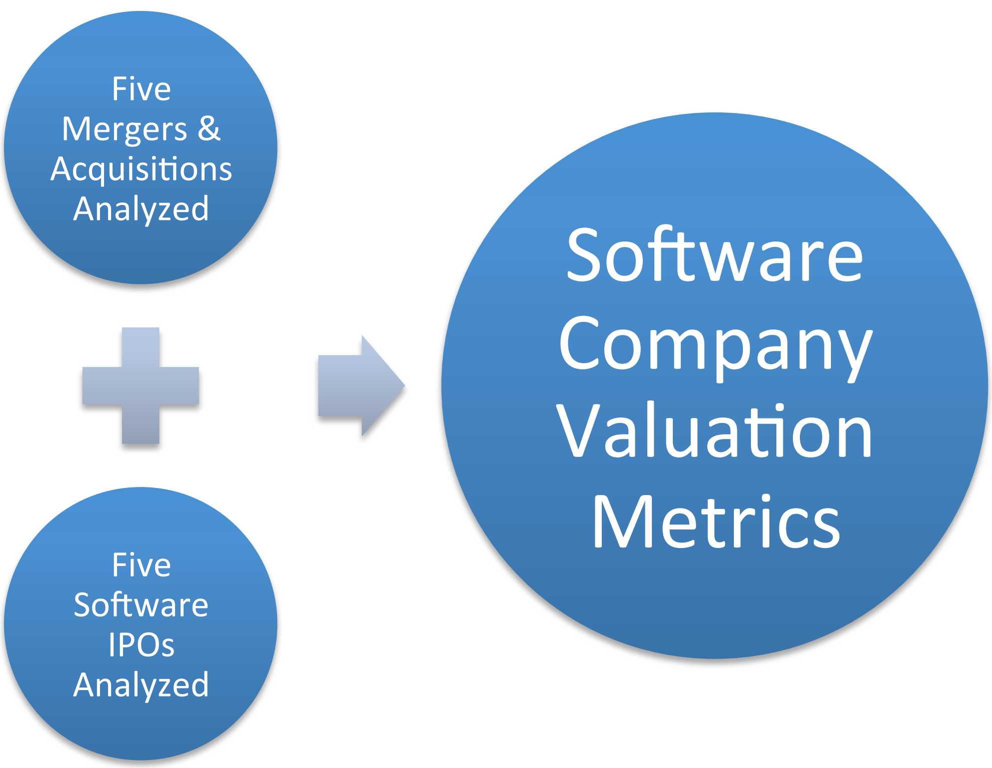
SOFTWARE CEO GUIDE:

Valuation Trends in Recent Software Transactions



From the Partners

Determining the valuation of private software companies is a complex process. The complexities include private versus public, growth, size, market, software type, niche compared to mass market, and profitability. The greatest challenge facing software owners is understanding equity value. There are a number of ways to determine a software company's value. The goal of our research (the "paper") is to provide software companies with meaningful guidance by reviewing effective ways to determine value through the analysis of selected software transactions that have taken place over the last 12 months combined with our experience as investment banking professionals. We hope that you will find this paper to be of interest and a useful resource.

SilverCloud Partners

Executive Summary

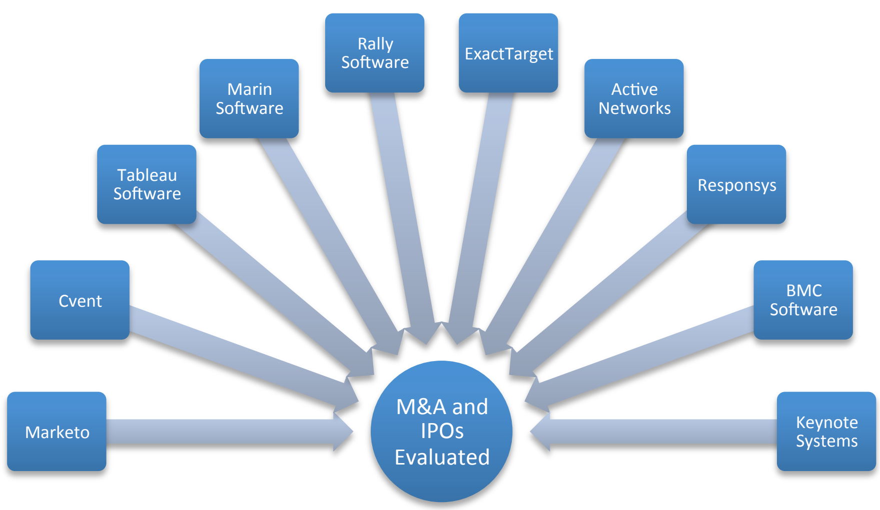
United States (US) equities have had significant growth over the last 12 months. Specifically, 2013 was the best year for the US equity markets in 16 years, see Bloomberg: "the broadest equity rally on record". [i] Strong equity markets lead to stronger activity in mergers & acquisitions (M&A) and initial public offerings (IPOs). Regarding M&A, in a recent Forbes article Jeff Golman states: "Healthy stock market performance – the S&P 500 was up nearly 30 percent in 2013 – which may push companies to demonstrate sustained growth through M&A to validate share prices". [ii] According to a recent survey by KPMG: "the United States is expected to experience the highest level of M&A activity in 2014". Accordingly, SilverCloud Partners (SCP) offers insights and guidance for software companies as they explore their strategic alternatives. Our insights and guidance are based on selected transactions from the past 12 months. This paper covers ten transactions involving selected software companies, primarily niche providers of business to business (B2B) software and explores various valuation methods as well as facts and information about each transaction. The purpose of the paper is to provide information to software companies regarding the current environment for capitalizing on the value of their equity.

Introduction

According to KPMG's research, [iii] 2014 should be an active market for software company transactions. Transactions are defined as selling ownership/equity, which is typically accomplished through mergers & acquisitions, selling equity to the public market (IPO) or selling equity in a capital raise. This report focuses on two of the three examples above outlined, M&A and IPOs from a valuation perspective. As KPMG's research suggests most transactions in 2014 will be small to middle market with 75% of all transactions valued at less than $250M. As a boutique investment banking firm focusing primarily on small to middle market software companies, SCP's goal is to provide guidance to the market and software companies through the exploration of various valuation multiples.

Objectives

The objective of this paper is to provide information on how software companies are currently being valued by analyzing notable M&A transactions and the IPOs that have taken place over the past 12 months. This will give guidance to private software companies with regard to their potential value and the various valuation methodologies being used. The following is an analysis of five selected M&A transactions and software IPOs. The transactions were selected as representative software companies across various markets and sizes, which SCP believes to be the most representative for the companies in its business sector.



Methodology

The following figure illustrates the process developed by SCP used in evaluating the valuation multiples of the representative software companies.

In our analysis, we made the following calculations to determine transaction multiples:

Trailing 12 Months Revenue (TTM) Multiple: is calculated based on the SEC quarterly/annual filings for each company. To determine a calendar year amount, estimates or approximations may have been necessary. The TTM calculated on an annual basis is divided into the total purchase price as disclosed to obtain the multiple.

Forward 12 Months Revenue (FTM) Multiple: is calculated based on the SEC quarterly/annual filings for each company along with assumptions based on the estimated growth rate per quarter. To determine a calendar year amount, estimates or approximations may have been necessary. The FTM once calculated on an annual basis is divided into the total purchase price to obtain the multiple.

Recurring Revenue (RR) Multiple: is calculated based on the SEC quarterly/annual filings per company. In determining the calendar year amount is estimate or approximations may have been used. The RR calculated on an annual basis is divided into the total purchase price to obtain the multiple.

Gross Profit (GP) Multiple: is calculated based on the SEC quarterly/annual filings per company. To determine the calendar year amount estimates or approximations may have been made. The GP calculated on an annual basis is divided into the total purchase price as disclosed to obtain the multiple.

Finally, we reviewed growth rates and profitability as differentiators to gain an understanding of why some companies received higher valuations. As expected, the companies with high growth and strong profit margins obtained the highest multiples.

Analysis

ExactTarget

In July of 2013 Salesforce acquired ExactTarget for approximately $2.5 billion. At the time it was the largest transaction in Salesforce.com's history and was its 8th transaction over the past year according to the Indianapolis Business Journal. [iv] ExactTarget was a major acquisition for Salesforce.com and fit in its strategy of adding marketing tools to its leading sales force automation software service. At the time of the acquisition, TTM was approximately $317M. The $2.5B purchase price represented an approximate 50% premium to the stock price at the time of the announcement. CEO Marc Benioff believed the addition of the email and digital marketing campaign functionality via ExactTarget was an excellent addition to previous acquisitions, Radian6 and Buddy Media. The acquisition allowed Salesforce.com to continue to acquire technology for chief marketing officers of organizations and allowing Salesforce.com to compete with other groups like Oracle, Constant Contact and Mailchimp in this category. Salesforce.com viewed this as a strategic transaction and structured its purchase price accordingly. ExactTarget was not profitable at the time of the acquisition, however the transaction was valued at approximately 7.9X TTM revenues. This was the largest sales price of the ten transactions evaluated.

Transaction Value

2.5B

Revenue (TTM)

317M

Profitability

Negative

Market

(Niche) Multi Channel Digital Marketing Software

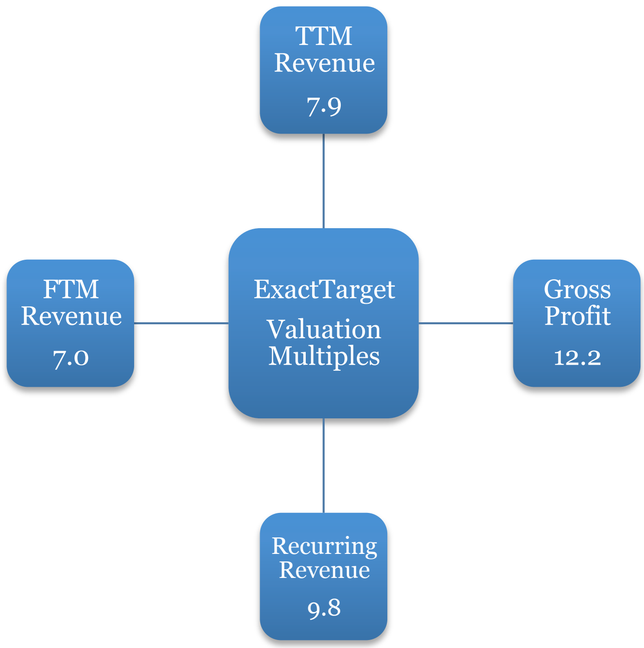
Strategic Buyer

SalesForce.com

ExactTarget is a leading Cloud Marketing Platform with an estimated 6,000 customers and was founded in 2000. Their solutions enable marketers to integrate customer data from any source to power digital marketing campaigns across multiple channels leveraging sophisticated marketing automation capabilities. Key accounts include Coca-Cola, Gap and Nike. [v]

Salesforce.com is a provider of enterprise cloud computing solutions delivering customer relationship management (CRM). It provides four core services—Sales Cloud, Service Cloud, Marketing Cloud and the Salesforce1 Platform. Their customers include all sizes of companies in almost every industry worldwide. Through their platform and other developer tools, they encourage third parties to develop additional functionality and new apps to run separately or in conjunction with their services. [vi]

Transaction Multiples



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In September 2013, Vista Equity Partners ("Vista") acquired The Active Network, Inc. for approximately $1 billion. At the time, it was the fourth largest software deal announced by Vista over the last 12 months. [vii] Vista's acquisition strategy focuses on companies that have high recurring revenue through well-established technology services. The Active Network transaction provided an opportunity for Vista to restructure the business and operate it as a private company. "There's an opportunity to clean it up away from the public eye," RBC Capital Markets analyst Andre Sequin told Bloomberg BusinessWeek. [viii] At the time of the acquisition, TTM revenue was approximately $465M. The $1B purchase price represented an approximate 27% premium above the stock price at the time of the announcement. Vista appears to have paid a reasonable price for Active based on the valuation multiples of the transactions evaluated. If Vista is able to move Active to profitability, it is positioned to obtain a strong return on its investment. The market for activity and participant management software presents the opportunity for consolidation that supports future growth. Active was not profitable at the time of the acquisition and Vista valued it at approximately 2.3X TTM revenues. This is the lowest sale price of the ten transactions evaluated in this paper.

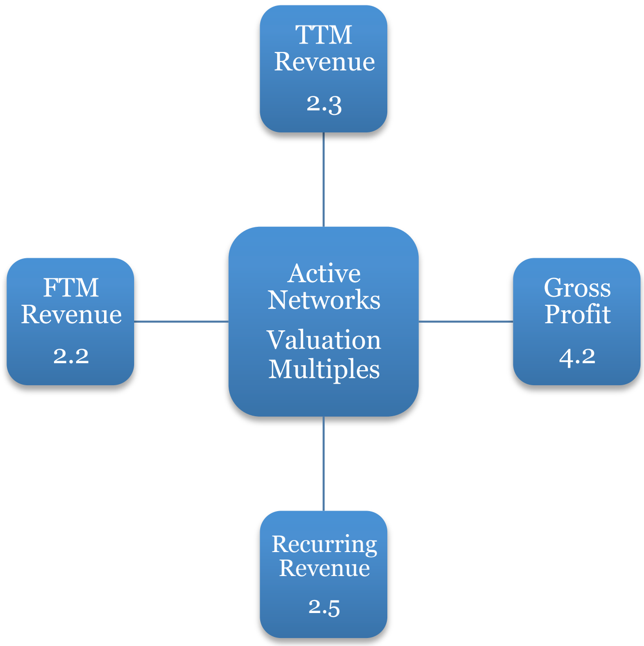
Transaction Value	Revenue (TTM)	Profitability
1B	465M	Negative

Market	Financial Buyer
(Niche) Activity and participant management software in the cloud	Vista Equity Partners

The Active Network is a leading provider of Activity and Participant Management™ solutions. The ACTIVE Works cloud platform scales to meet the needs of its customers, large and small, and makes managing and operating all types of activities, events and organizations efficient. They have approximately 55,000 global customers using vertical technology applications for their markets.

Vista Equity Partners is a private equity firm with approximately $7.7 billion in cumulative capital commitments. It concentrates on software business models and has developed specific operational improvements to create value, and combine this operational capability and experience with a long-term perspective. This combination intended to promote optimal business decisions, enable the pursuit of operational excellence, and ultimately create value for shareholders. Vista is a low volume, high value-add firm that makes a limited number of investments per year. Vista's investment process attempts to identify specific companies that can be acquired and transformed into predictable, high cash flow businesses. [ix]

Transaction Multiples



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bmcsoftware

In May 2013, a private investor group led by Bain Capital and Golden Gate Capital together with GIC Special Investments Pte Ltd ("GIC") and Insight Venture Partners agreed to acquire BMC Software for approximately $6.9 billion. At the time, Bob Beauchamp, Chairman and Chief Executive Officer at BMC stated: "BMC believes the opportunity to become a private company will provide additional flexibility and position us to invest more strategically to drive powerful innovation and deliver cutting edge customer solutions. We look forward to working closely with all parties to complete this transaction and enter into our next chapter of growth and industry leadership." At the time of the acquisition TTM revenue was approximately $2.2B. The stock had climbed 13% since March based on anticipation of a potential transaction. The private investor group most likely saw value in the large amount of recurring revenue and significant EBITDA generation. With debt still remaining fairly inexpensive private equity firms can gain leverage to do large deals, like BMC software. Especially where the target is profitable with strong cash flow.

Transaction Value

6.9B

Revenue (TTM)

2.2B

Profitability

Positive

Market

(Mass Market) IT management software

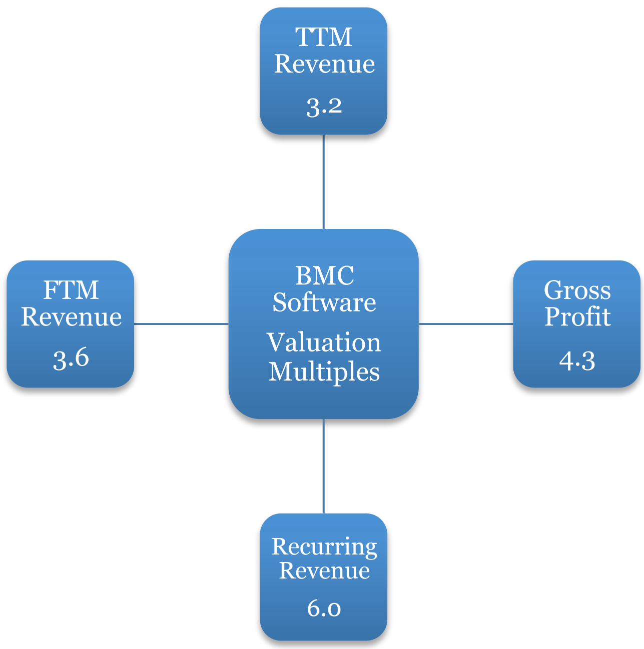
Financial Buyers

Bain Capital
Insight Venture Partners
Golden Gate Capital
GIC

BMC Software aids companies around the world to put technology at the forefront of business transformation, improving the delivery and consumption of digital services. From mainframe to cloud to mobile, BMC delivers innovative IT management solutions that have enabled more than 15,000 customers to leverage complex technology into extraordinary business performance by increasing their agility.[x]

The Private Investor Group - Insight Venture Partners is a global private equity and venture capital firm founded in 1995. It has raised more than $7.6 billion, invested in more than 190 companies. [xi] Golden Gate Capital is a privately held enterprise with over $12 billion in committed capital. It operates as a private holding company and helps to recapitalize, restructure, and ultimately build meaningful businesses in partnership with management over an indefinite time horizon. [xii] Bain Capital Private Equity partners along with management teams provides the strategic and analytic resources needed to build and grow companies. Since 1984, Bain has made over 250 investments that have generated industry leading returns while building a global network of highly trained team members. [xiii] GIC was incorporated in 1981 under the Singapore Companies Act and it is wholly owned by the Government of Singapore. It manages funds on behalf of the Government of Singapore, its sole client. [xiv]

Transaction Multiples



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keynote™

In August 2013, Thoma Bravo completed its acquisition of Keynote Systems (Keynote) for approximately $395 million. Orlando Bravo, the CEO of Thoma Bravo, stated: "The ever-changing online experience and the growth of the mobile market offer new and exciting opportunities for Keynote. We look forward to partnering with the executive team at Keynote to enable the company to accelerate growth and more quickly develop and acquire innovative solutions that meet customers' needs." [xv] At the time of the acquisition TTM revenues were approximately $125M and the $20 price represented a 48% premium over the stock price at the time the acquisition was announced. As a financial buyer, Thoma Bravo viewed Keynote Systems as a profitable niche subscription based software provider that was undervalued in the public market. Keynote has strong recurring revenue and EBITDA generation, which are always attractive considerations when private equity firms are evaluating financial transactions.

Transaction Value

395M

Revenue (TTM)

125M

Profitability

Positive

Market

(Niche) Cloud testing and monitoring software

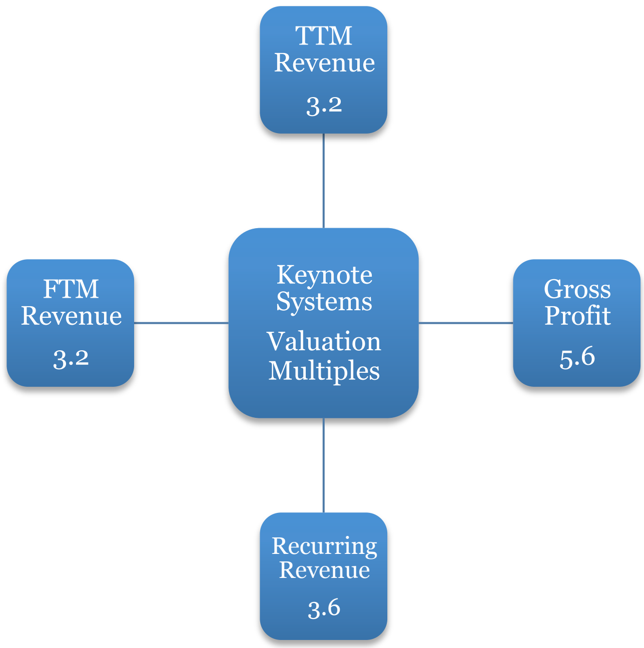
Financial Buyer

Thoma Bravo

Keynote is a global provider of Internet and mobile cloud testing & monitoring software. The company maintains on-demand performance monitoring and testing infrastructure for Web and mobile sites comprised of over 7,000 measurement computers and mobile devices in over 275 locations around the world. Keynote currently collects over 700 million mobile and Web performance measurements daily. Known as 'The Mobile and Internet Performance Authority™,' Keynote offers three market-leading product platforms: Keynote Perspective® provides on-demand performance monitoring for enterprise Web and mobile sites including online portals, e-commerce sites and B2B sites. Over 2,000 customers rely on Keynote Perspective services to know how their websites, content, and applications perform on browsers, networks, and mobile devices. Keynote DeviceAnywhere® is a cloud-based software platform for automated QA testing and monitoring of mobile applications and websites on smartphones and tablets. DeviceAnywhere is used by over 1,000 mobile enterprises and developers. Keynote SIGOS® offers active end-to-end Quality of Service (QoS) testing and monitoring solutions for mobile, fixed and VoIP communications. Its SITE and Global Roamer products are used by over 200 network operators, content providers, carriers and regulators in over 100 countries worldwide. Keynote's 4,000 customers include AT&T, Disney, eBay, E*TRADE, Expedia, Google, Microsoft, SonyEricsson, T-Mobile and Vodafone.[xvi]

Thoma Bravo is an experienced private equity firm providing equity, strategic and operating support to businesses and their management teams for more than 30 years. Their investment strategy is based on the concept of "industry consolidation" or "buy and build" investing which creates value through operational improvements, internal expansion, and the strategic use of acquisitions to accelerate earnings growth. Their investment process involves identifying and becoming deeply knowledgeable about industry sectors which are fragmented and consolidating and investing in businesses in those sectors that can grow both organically and by acquiring and integrating similar businesses. They apply this investment strategy and process across multiple industries with a current focus on application and infrastructure software, business and financial services, education, and media. With offices in Chicago and San Francisco, Bravo invests principally in the United States, but considers global opportunities as well. [xvii]

Transaction Multiples



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responsys

In December 2013, Oracle acquired Responsys for $27 a share resulting in a $1.5 billion valuation, a 38% premium. "Our strategy of combining the leaders across complementary technologies signifies Oracle's overwhelming commitment to winning and serving the C.M.O. better than any other software company in the world," said Oracle's President, Mark Hurd, referring to chief marketing officers. [xviii] At the time of the acquisition, TTM revenue was approximately $194M. Responsys was acquired for a 7.7 multiple of TTM revenues (comparable to the multiple in the ExactTarget transaction) as Oracle was a strategic buyer and mostly desired to keep up with SalesForce.com in the CRM market. Niche marketing automation software appears critical to CRM and SFA solutions, which are a major focus of both companies.

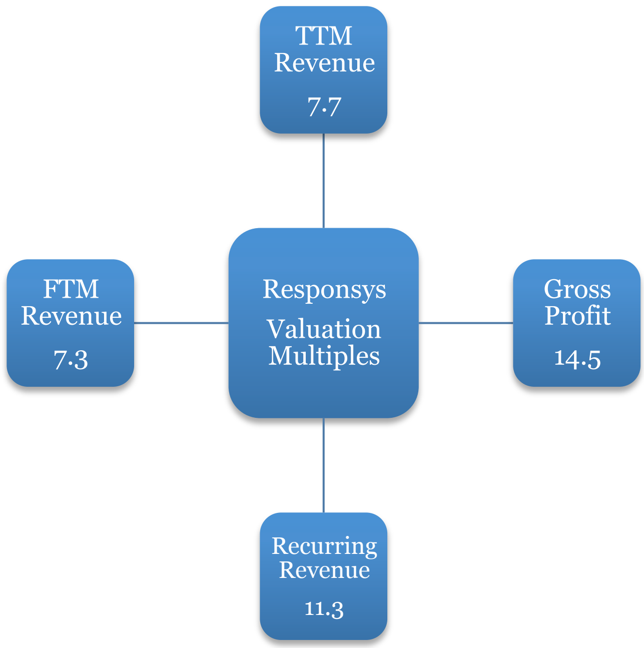
Transaction Value	Revenue (TTM)	Profitability
1.5B	194M	Negative

Market	Strategic Buyer
(Niche) Marketing cloud software	Oracle

Responsys is a niche provider of cloud marketing software and services. Its mission is to enable smart marketing in the digital world. Many respected brands across the globe use the Responsys Interact Marketing Cloud to manage their digital relationships and deliver the right marketing information to customers via email, mobile, social, display and the web. Founded in 1998, Responsys is headquartered in San Bruno, California and has offices throughout the world. [xix]

Oracle is a mass-market software provider that concentrates on shifting the complexity from IT, moving it out of the enterprise by engineering hardware and software to work together in the cloud and in the data center. By eliminating complexity and simplifying IT, Oracle enables its customers, 400,000 of them in more than 145 countries around the world, to accelerate innovation and create added value for their customers. [xx]

Transaction Multiples



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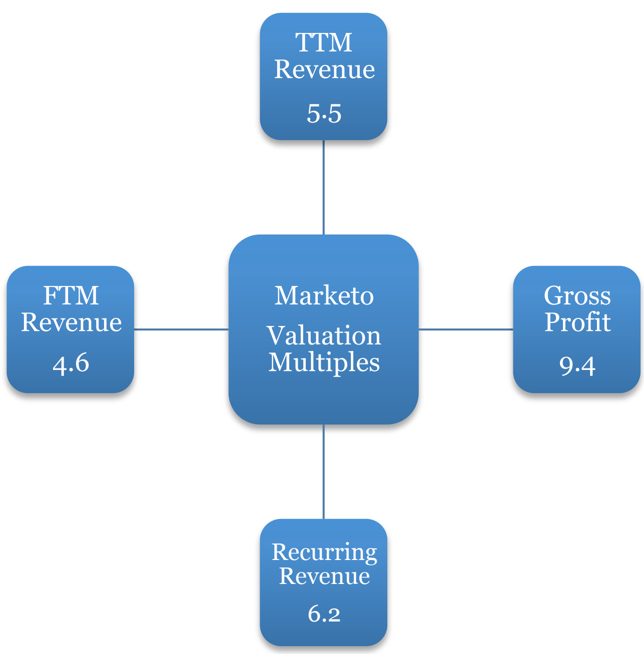
Marketo

In May 2013, Marketo became publically traded and raised approximately $80 million giving it a market capitalization of $724 million on the first day of trading. [xxi] At the time of the offering, TTM revenue was estimated to be $143M. As with most initial public offerings, the primary purpose was to increase financial flexibility, improve visibility in the marketplace and create a public market for shares. Net proceeds were to be used for working capital, general corporate purposes and capital expenditures and in addition fund opportunities from time to time to expand their current business through acquisitions of or investments in complementary companies, products or technologies. The marketing automation software niche is “hot” as both ExactTarget and Responsys were acquired and received strong valuation multiples. Marketo took a different approach by going public and raising capital to continue its growth path and perhaps command a higher valuation [xxii] in a future acquisition. [xxiii]

Marketo is a niche software provider of marketing automation software that is fundamentally different from other kinds of business applications, like CRM or ERP. With those systems, companies typically configure them once, and then use them for months or even years with little change. Marketing is much more dynamic since users need to conceive, build and launch new marketing campaigns every few days or weeks, with minimum effort and with little or no IT support. And with CRM integration capabilities, the common experience extends to a sales team and the customers they communicate with. Looking inward toward the marketing user, Marketo combines completely integrated tools for multi-channel campaign management, social marketing automation, event management, inbound marketing, and customer data management using powerful analytic tools. Combined with its global partner network it has more than 2,500 customers in 36 countries around the world. [xxiv]

Transaction Multiples



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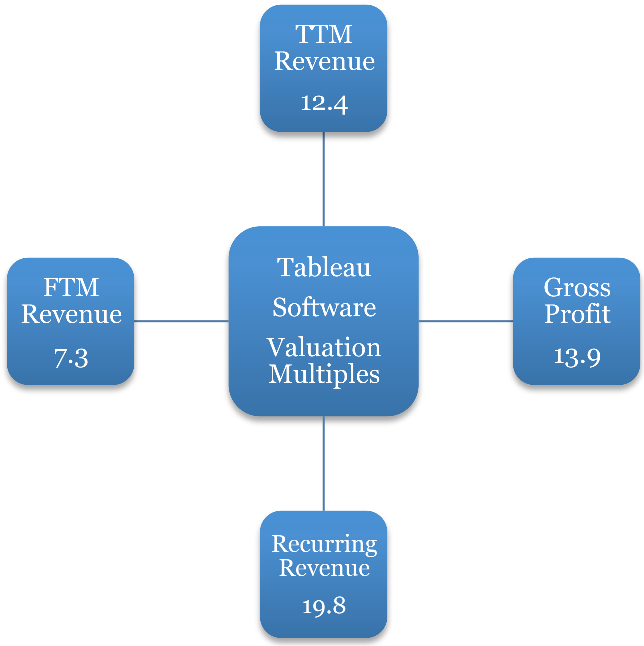
In May 2013 Tableau Software became publically traded and raised $254 million giving it a market capitalization of approximately $2 billion. [xxv] At the time of the IPO, TTM revenue was approximately $143M. The stated purpose of the IPO was to increase the company's financial flexibility, improve its visibility in the marketplace and create a public market for its shares. As documented in the S-1, the company intended to use of the net proceeds for working capital, general corporate purposes and capital expenditures and in addition to fund opportunities from time to time to expand their current business through acquisitions of or investments in complementary companies, products or technologies. Tableau received the highest multiples of the companies evaluated in this paper. They provide software for the frenzied market of data visualization and business intelligence and have shown the ability to obtain significant growth while generating profits. [xxvi]

Tableau Software is a niche computer software provider of interactive data visualization products focused on business intelligence. Their mission is to help businesses understand their data. In 2020 the world will generate 50 times the amount of data generated in 2011 and 75 times the number of information sources (IDC, 2011). Within this data are huge, unparalleled opportunities for human advancement, however in order to turn these opportunities into reality, businesses need the power of data at their fingertips. Tableau builds software to deliver the data in real-time. Their products transform the way people use data to solve problems. [xxvii]

Transaction Multiples



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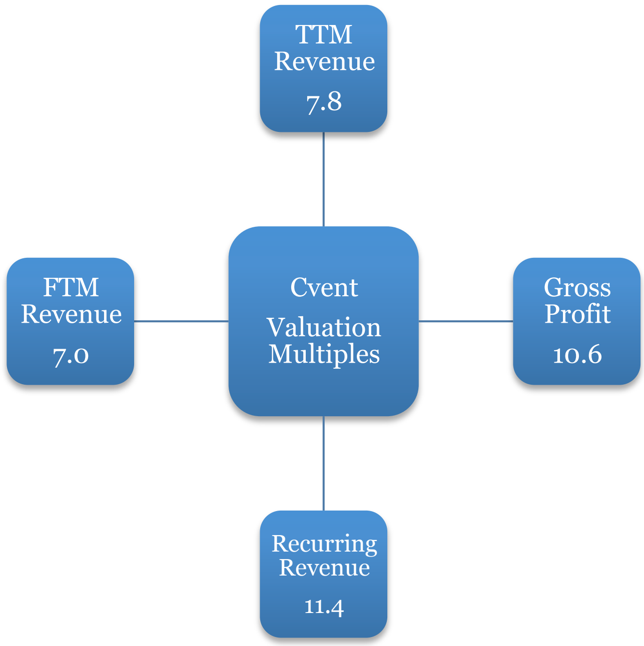
In August 2013, Cvent entered the public markets and raised approximately $118 million giving it a market cap of $1.5 billion and a TTM revenue multiple of 7.8x at the time of the pricing of the IPO. [xxviii] At the time of the IPO, TTM revenue was approximately $104M and the company was marginally profitable on an EBIT basis. As with most IPOs the stated purpose of the offering/funding was to create a public market for the company's common stock and provide efficient access to future capital. Cvent intends to use the proceeds from the initial offering for working capital, expansion of their operations, product development and acquisitions in complementary technologies. Cvent was marginally profitable at the time of the offering and had a modest growth rate. The IPO probably allowed the private equity funds that were significant owners to gain liquidity via the public currency. In addition, the capital will provide the company with the resources to potentially accelerate growth. The events software space, although still very much a niche has been gaining more attention and visibility. [xxix]

Cvent is a niche provider of web-based event management, venue sourcing, and strategic meetings management software with 187,000 users in 90 countries. It was established in 1999 with an event management offering and now has a number of other web-based software applications, including the their Supplier Network product that connects meeting planners with 200,000 event venues and service providers globally.[xxx]

Transaction Multiples



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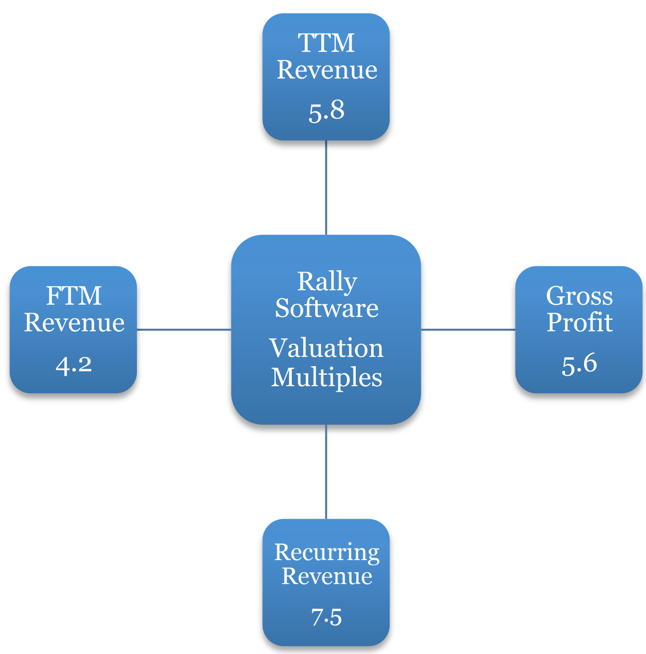
In April 2013 Rally Software went public and raised approximately $84 million giving it a market cap of $314 million and a TTM revenue multiple of 5.8x. [xxxi] At the time of the acquisition, TTM revenue was $57M. As disclosed in the S-1, the primary purpose of the offering was to increase financial flexibility, improve visibility in the marketplace and create a public market for its shares. Uses for the net proceeds were stated to be working capital, general corporate purposes, data center infrastructure investments, expanding the sales force and increasing international presence. In addition, to provide funding to take advantage of opportunities from time to time to expand the current business through acquisitions or investments in complementary companies, products or technologies. Rally is in the niche software space of agile software development. Rally received a reasonable multiple although they were on the small side of a companies going public. In spite of the cost and pressures of being public, they are maintaining strong growth rates. At the time of the offering they were not profitable. Strategically, they may be an acquisition target by a larger software development tools company, especially if they continue to grow and trend toward profitability. The IPO was a branding opportunity and a way of increasing capital to help maintain the growth rate. [xxxii]

Rally Software is dedicated to making a company run faster, leaner and more Agile from a software development perspective through the use of their products. They are an Agile partner with a team of Agile coaches and comprehensive training services that help teams and leaders navigate the organizational change required to become an Agile business. Forrester Research stated: "Rally's leadership rests with its breadth and depth of capabilities for Agile teams, combined with a strong and focused corporate strategy." Rally serves 192,000 users, including 34 of the Fortune 100 companies.[xxxiii]

Transaction Multiples



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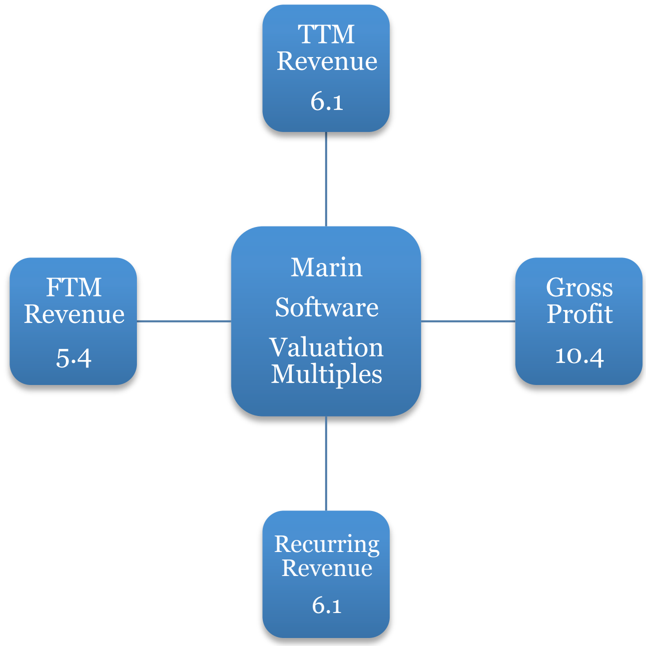
Marin SOFTWARE

In March 2013, Marin Software became publically traded and raised approximately $105 million giving it a market cap of $400 million and a TTM revenue multiple of 6.1x. [xxxiv] At the time of the offering, its TTM revenue was approximately $71M and the company was not profitable. Marin's reason for going public was to increase its ability to raise capital, improve visibility in the marketplace and create a public market for its shares. Uses of the net proceeds were stated to be working capital, general corporate purposes and increasing market exposure. Additionally, it provided funds to potentially expand the business through acquisitions or investments in complementary businesses or technologies. The company is not expected to begin making a profit until 2015. From 2009 to 2012 Marin grew from $8 million to almost $60 million with a negative EBIT of approximately $25 million. [xxxv]

Marin Software is a San Francisco-based niche software company whose product allows marketers to track and optimize paid advertising campaign performance on multiple platforms, including Google, Bing, Facebook, and Baidu. Its customers (University of Phoenix, Macy's, Razorfish, Neo@Ogilvy, PriceGrabber, Symantec and Salesforce) rely on Marin's software platform to manage approximately $6B in ad spend annually. [xxxvi]

Transaction multiples



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Results/Conclusion

Company/Multiples	TTM	RR	FTM	GP	Profitable
Active Network	2.3	2.5	2.2	4.2	No
BMC software	3.2	6.0	3.6	4.3	Yes
Cvent	7.8	11.4	7.0	10.6	Yes
ExactTarget	7.9	9.8	7.0	12.2	No
Keynote Systems	3.2	3.6	3.2	5.6	Yes
Marin Software	6.1	6.1	5.4	10.4	No
Marketo	5.5	6.2	4.6	9.4	No
Rally Software	5.8	7.5	4.2	5.6	No
Responsys	7.7	11.3	7.3	14.5	Yes
Tableau Software	12.4	19.8	7.3	13.9	Yes

→ Growing B2B niche software companies produce the highest valuation multiples from a M&A perspective. Specifically, ExactTarget and Responsys both received greater than a 7x multiple on TTM revenue notwithstanding their lack of profitability.

- → Financial buyers produced lower transaction multiples for M&A transactions as TTM revenue multiples were between 2.2X and 3.2X.
- → The TTM valuation multiples for the 5 IPO's evaluated ranged from 5.5X to 12.4X. This is interesting, as these new to the public market software companies received strong valuations, especially compared to mature software companies like Google or Facebook that are valued at 7x [xxxvii] and 21x [xxxviii] TTM revenue, respectively.
- → The software companies evaluated from an IPO perspective were small for public company benchmarks, but their high valuation multiples anticipate future growth. The level of profitability of the IPO's evaluated other than Tableau and to a lessor extent Cvent was not profitable on an EBIT basis.
- → The M&A transactions included two companies that were profitable at an EBIT level, BMC Software and Keynote Systems. ExactTarget and The Active Network had negative EBIT and Responsys was break-even.
- → The growth rates based on TTM revenue were much stronger for the IPO group when compared to the M&A group.

As software companies review this analysis to obtain a sense of their potential valuations, it should be noted that the ten companies evaluated were public. A public software company commands a higher valuation as compared to a private company. The various valuation multiples and methods if used as benchmarks should be evaluated along with the company's historical growth rate, profitability levels, size, market niche and mix of revenue (recurring versus non-recurring). In addition, the ten companies evaluated have been highly successful in their respective markets. The evaluations for these companies can be used as guidelines; however, every company's valuation differs based on market factors.

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Endnotes

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