Investment Trends in the IT Industry

Follow the Money in Technology Business

GTDC

Quick Links

About the Report 3

Investors Double Down on Information Technology Businesses 4

Who Are the IT Investors? 6

Identifying the Investment Groups 9

Top Technology Investment Targets 10

Recent Investment Activity in Distribution 11

A Positive Forecast for IT Investments 12

Potential Challenges 13

Can Distribution Affect IT Investment? 14

About the Report

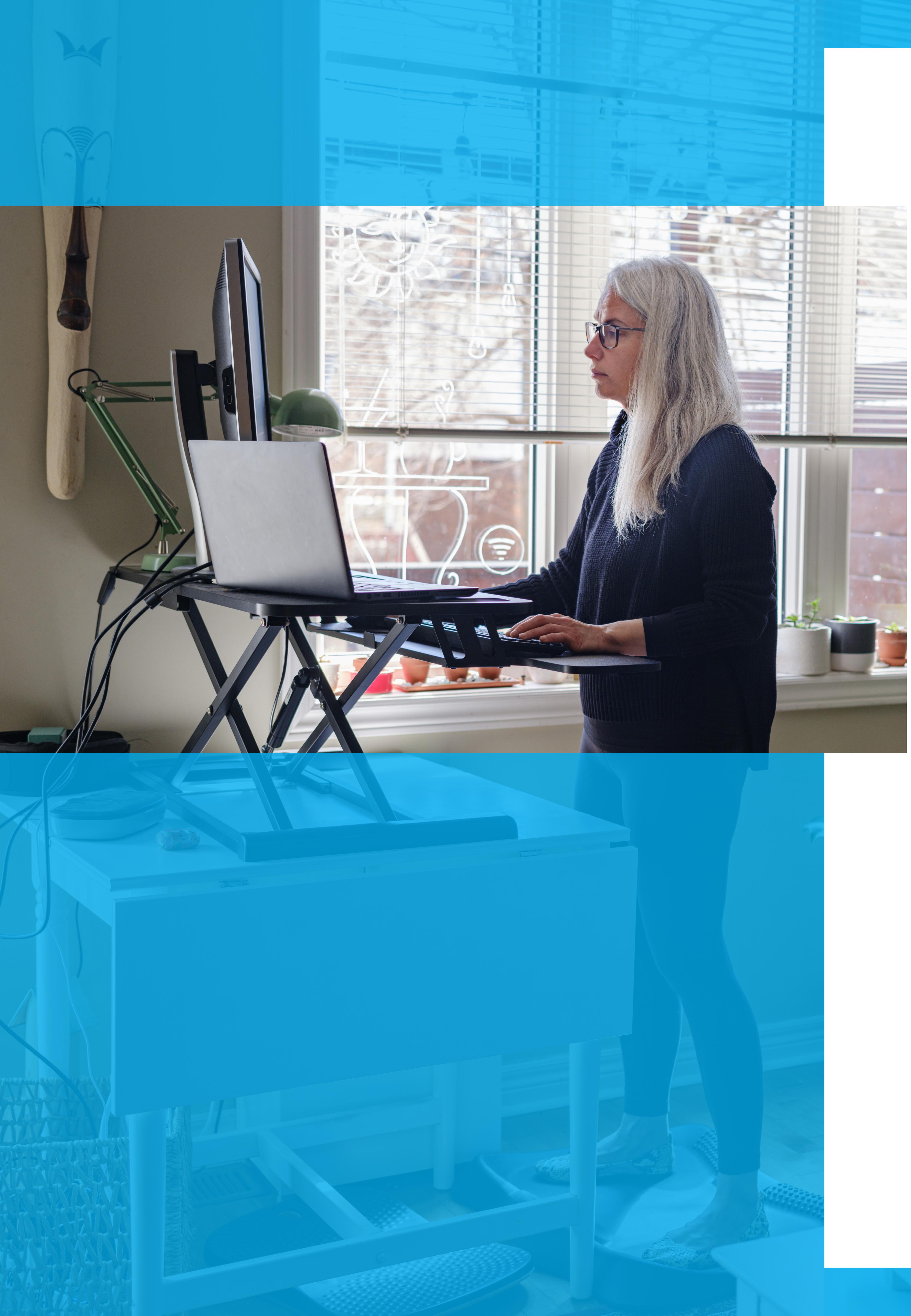
The information technology space is hot. That statement may be on the more conservative side of estimates based on the investment dollars that continue to pour into the industry and confidence from analysts and speculators that those trends will continue. IT companies are attracting more investment dollars with the increasing importance of technology in business operations, heightened by the shift to working from home and hybrid environments and ongoing labor shortages.

While inflation and interest rate changes may spur economic concerns, strong demand in most technology sectors continues to gain even more attention from risk-averse shareholders, venture capitalists and private equity firms. Whether looking to diversify or strengthen portfolios, the investment community is betting heavily that these companies will continue to experience robust financial performance, and the trends are in their favor.

For example, despite the pandemic and worldwide economic and labor challenges, global venture investment in the technology industry hit a record USD 643 billion in 2021. That number represents a whopping 92% growth rate year-over-year compared with 2020 (USD 335 billion). Industry financial experts suggest those positive trends should continue considering the growth of private equity funds and the number of opportunities available in the tech community.

This GTDC report explores the drivers of investment. In addition to defining and providing examples of these activities, this study examines factors attracting investors to the technology industry, current and future trends, and global disparities.

Investment Trends in the IT Industry was commissioned by the Global Technology Distribution Council, which consists of the world's leading IT and ICT distributors. GTDC members drive approximately $150 billion in product and services business annually. The content was shaped based on timely input from industry researchers and an extensive 3rd-party analysis conducted in June and July 2022. For more information on GTDC research, visit the organization's Knowledge Hub.



Investors Double Down on Information Technology Businesses

IT fuels businesses today. Computing devices and other technology solutions are the cornerstone of operations for virtually every organization, and the workplace changes brought about by the pandemic highlighted that narrative. Whether adopting temporary WFH environments or permanently shifting office policies, many companies recognized the value of their past IT investments and began exploring short- and long-term upgrades. Many members of the information technology industry deserve accolades for their efforts to keep people connected and businesses operational during the pandemic.

That foundational organizational value is directly connected to current and future success. While information technology companies have been attracting investors' dollars since the introduction of the first computer, activities over the past two-plus years have heightened awareness and the business case of high-tech firms.

Cloud applications' steady growth and earnings power also garner a fair share of attention. Recurring revenue streams generate predictable cash flow and offer greater financial assurances to potential investors. The 'as a service' model removes some mystery for current and prospective stakeholders by making it easier to calculate revenue and profit projections since prices and associated discounts are typically fairly standard. Assuming the organization can scale those services without incurring significant new costs, projecting sales and profit potential is a simple matter of multiplication. Estimating the value of other organizations, including those that manufacture hardware, components, and ancillary products can be more complicated.

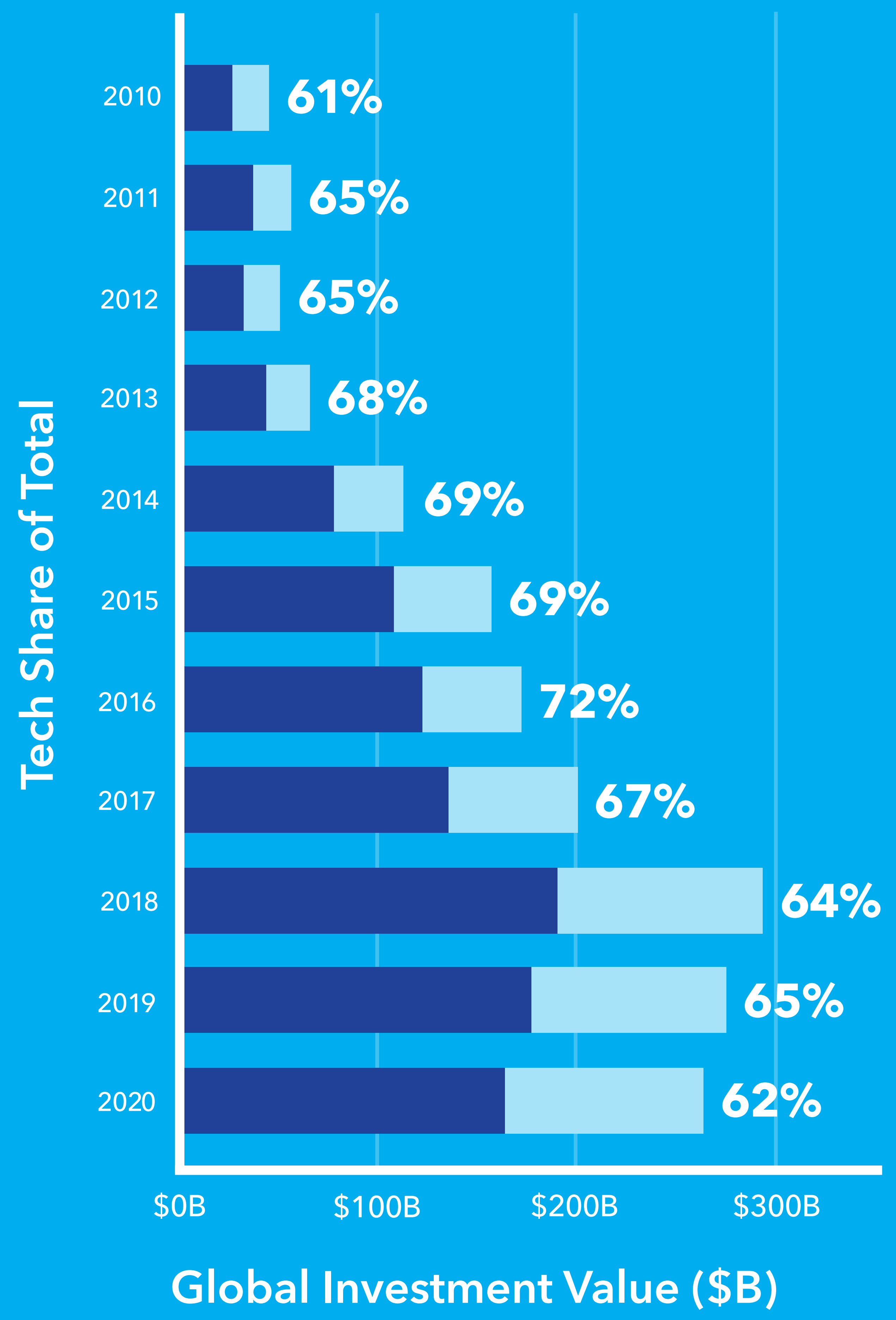
Even without the simplified math options, investors see information technology companies as value drivers. IT firms represent steady revenue growth potential. While technology may not be completely recession-proof, even during some of the worst economic conditions, businesses and individuals continue to purchase computers and devices and procure software or cloud applications. As inflation and labor costs rise, companies invest in automation and productivity solutions such as Customer Relationship Management (CRM), Enterprise Resource Management (ERP) platforms, and project management tools.

Technology empowers workers, reduces overall operational costs and allows companies to deliver new and better services to their customers. Investors understand that value proposition, and nowhere is that more apparent than in the global venture capital community. According to research by Bain & Company, between 2010 and 2020, most of those investments – between 61% and 72% – went to technology companies.

Companies with solid business metrics that manufacture, develop, and/or deliver resource-saving technologies tend to rank high on the list of potential M&A and funding candidates. Despite the wealth of business uncertainties over the past couple of years, the financial resources available to IT companies are growing rapidly today. That study also notes that while the value of total investments in high-tech decreased 13% from 2018 through 2020 amid an overall decline in VC activity—the first drop since 2012—those numbers rose quickly and significantly amidst the COVID-19 pandemic.

Digital transformation and flexible workplace models are major contributors to that growth. SaaS companies are attractive investment targets as businesses adapt and shift more of their IT budgets to cloud solutions, driving even higher recurring revenue streams (and valuations). The explosive growth of digital applications and cybersecurity solutions, the Internet of Things (IoT) and Artificial Intelligence-enabled systems make the high-tech industry an attractive opportunity for knowledgeable investors.

Tech Companies Consistently Receive the Majority of Venture Funding



Notes: Includes investments by independent venture capital firms and corporate venture capital funds; excludes private equity investments.
Sources: Crunchbase; Bain Startup Investment Cruncher analysis.

Global Gross Domestic Savings

$23.82 Trillion
(2019)

$22.88 Trillion
(2020)

Who Are the IT Investors?

Businesses and individuals save a staggering amount of money each year. According to the World Bank, in 2020, global Gross Domestic Savings – the money households, private corporations and the public sector have left after paying expenses each year – was approximately $22.88 Trillion, a drop from a record $23.82 Trillion the previous year. That means a significant amount of cash is available for people and organizations to save or invest. From individuals, banks and retirement plans to union funds and business profits, most decision-makers will look for safe ways to maximize their earnings on those reserves.

The good news is that investment options are plentiful today. While venture capital and private equity gain a lot of attention in the IT industry based on high-profile mergers and acquisitions involving those firms, those are not the only funding sources available for IT-related businesses. Some of the more common investors in information technology businesses include:

- **Private Equity (PE)** - These funds usually involve a limited group of investors who purchase privately held businesses or acquire control of publicly-traded companies. Their objectives are typically to invest in organizations with unrealized growth potential to turn around or expand the business. PE firms frequently take publicly-traded organizations private to remove normal market scrutiny and stock pricing pressures while restructuring to turn around or grow the business. At that point, those companies are often sold for a profit. Private equity may refer to funds, firms or limited partnerships made up of pension plans, university or community endowments, wealthy individuals or families and other businesses. The firm typically serves as an "entity" or lead throughout all the various processes.

- **Venture Capital (VC)** - Financial experts consider these firms or funds as part of the higher-risk segment of the private equity market. VC investors typically target companies in the early or startup phase, smaller organizations that present high growth potential. Despite the greater risk, the promise of above-average returns is a draw for a growing segment of the investment community. Emerging technology companies often explore venture capital markets to fuel rapid expansion plans and bolster their sales and marketing efforts. The biggest drawback of VC is that investors may receive equity and influence in management decisions, including approval of executive hires or seats in the boardroom.

- **Angel Investments** - This funding community consists of affluent people leveraging their own capital to steady and grow businesses in the early stages of development. Most angel investors receive equity and potentially a say in the organization's management decisions and offer their expertise and guidance to assist in various aspects of the operations. According to the Angel Capital Association, approximately 90% of outside equity received by startups come from this part of the investment community.

- **Peer-to-Peer** - Also known as P2P or social investment, this typically involves loans, not ownership-type investments. The process involves pooling small amounts of money from different people via web platforms (or other means) that organizations can borrow for various purposes. Since these programs eliminate the middle people and some paperwork, the rates and fees are typically lower than banks. That lending model is a cost-effective option for startups and entrepreneurs looking for funding sources that won't require them to give up equity or control. Similar platforms allow individuals to receive dividends or shares from their pooled investments.

- **Banks** - This time-tested lending model remains a top commercial funding source. Banks' primary profits come from lending as much money as possible, charging higher rates to customers with higher risk profiles and less to those with more collateral, stronger credit histories and more proven business plans. While commercial loans can help IT companies fund expansion or bridge cash flow concerns, interest charges and other fees can be substantial. One benefit of these loans is that, as long as payments are current, the owners maintain complete control of the business (no loss of equity).

.

Common Investors In Information Technology Businesses Include

Private Equity

Venture Capital

Angel Investments

Peer-to-Peer

Banks

"Last year, there were fewer than 1,000 deals, and 2022 should easily top that mark."

– Joe Panettieri
Executive VP, CyberRisk Alliance

Major mergers and acquisitions can involve a mix of different investment types from the options listed above. From angel and peer-to-peer opportunities and individual financial backers to venture capital and private equity, some of the larger deals may include (if not require) multiple funding sources. PE firms also have a history of procuring companies that VC helped build, and those activities are rising.

The number of private equity firms acquiring startups fueled by venture capital funds increased approximately 18% per year from 2000 to 2019, according to PitchBook. Considering the annual growth rate of 9.5% for all buyouts during that period, the relationships between PE and VC companies appear to be flourishing. And the number of players and transactions seems to be climbing.

"Last year, there were fewer than 1,000 deals, and 2022 should easily top that mark," says Joe Panettieri, Executive VP at CyberRisk Alliance. "Most people don't realize how many private equity firms are in the market, but more than sixty of those investors have already been involved in transactions in 2022." Panettieri expects M&A activity across the MSP, IT services, cloud and distribution ecosystems to remain steady to strong through 2023. However, some deal valuations could be pressured as buyers reassess acquisition strategies amid inflation and rising interest rates.

Identifying the Investment Groups

The list of financiers and funds targeting the information technology industry is long and growing, but here are some firms that have been quite active in the IT community over the past few years:

- Accel Partners invests in organizations such as DocuSign, Dropbox, and Slack
- Apollo Funds, a global asset management firm, was central to the TD SYNNEX merger
- Eight Roads Ventures focuses heavily on Asian and European technology companies
- Hg Capital maintains a comprehensive portfolio of software and technology businesses
- Insight Partners provides funding for companies like Veeam, Kaseya and Mimecast
- KKR funds in equity, credit and real assets in the high-tech community
- Platinum Equity investments include the recent purchases of Ingram Micro and Cision
- Summit Partners provides guidance and support to firms like A10, McAfee and Continuum
- Thoma Bravo counts ConnectWise, Barracuda, and Sophos in its collective IT portfolio
- Sequoia Capital has investments in Square, Zoom and Drift
- Silver Lake has supported companies like Dell, VMware, SolarWinds and N-Able
- Vista Equity Partners has practices in security, telecom, and enterprise resource planning

By no means is this a complete list. While this covers some of the more recognizable investment firms providing funds, expertise and support to information technology companies, there are likely scores of other reputable financiers offering similar services and resources. Some investors, including peer-to-peer and angel funds, tend to maintain a lower profile and keep some, if not all, of their activities confidential.

Top Five Technology Segments
Receiving Investment Dollars in 2021

1. Fintech **$50.62B**
2. Data Intelligence **$31.21B**
3. Digital Health **$24.03B**
4. Cybersecurity **$18.28B**
5. Martech **$13.13B**

Source: Vation Ventures Research, 2022

Five Most Critical Current Concerns of CIOs

Cybersecurity
97.4%

Customer Experience
91.1%

Moving to the Cloud
87.9%

Data Management and Analytics
87.9%

Employee Engagement
85.4%

Source: 2022 Innovation Advisory Council Report, Vation Ventures

Top Technology Investment Targets

Business valuations can fluctuate significantly within the same industry, and IT is no exception. While each investment firm may have different objectives, most firms scrutinize current and future sales projections as well as the metrics related to profitability and cash flow. Some segments of IT fit the ideal profile better than others, like emerging technologies and SaaS companies specializing in high-growth vertical markets.

Which companies are gaining investors' attention today? The **top five technology segments receiving investment dollars in 2021** include:

1. **Fintech** – $50.62B
2. **Data Intelligence** - $31.21B
3. **Digital Health** - $24.03B
4. **Cybersecurity** – $18.28B
5. **Martech** – $13.13B

*Vation Ventures Research, 2022

Those numbers correlate closely with the top business priority for CIOs. Investors must understand the technology needs of commercial and, when appropriate, non-business customers of companies of interest. Will demand rise or fall? What technologies are currently undervalued or will likely command a premium in the future?

CIOs know the answers. Their role involves studying and leveraging the critical data points and developing business priorities based on internal and external factors. From customer preferences and habits to operational aspirations and limitations, CIOs help executive teams understand the current and future business environments. That information allows companies to develop more impactful short- and long-term plans.

Recent Investment Activity in Distribution

End-user concerns are fueling the growth of IT and driving new capital into business throughout the industry. Over the past several years, distributors have been involved in some of that activity, from mergers and acquisitions and PE and VC investments to first-time and additional rounds of public trading. Those activities run the financial gamut, and while some of the transactions can occur quietly and without publicity, there were several recent notable deals.

For example, in July of 2021, Platinum Equity completed its acquisition of Ingram Micro Inc. from HNA Technology Co., Ltd, a part of HNA Group, for around **$7.2 billion,** including **$5.9 billion** of equity value. Apollo Global Management made a **$5.4 billion** deal to purchase Tech Data the previous year and take the distributor private– and just fifteen months later, company executives entered into a pure-stock merger agreement with SYNNEX to create TD SYNNEX. Also, in 2021, DCC Technology acquired the Almo Corporation for approximately **$610 million (£462 million)** in a bilateral transaction with the Chaiken family.

Distributors also used other financial means to boost investments. Exclusive Networks went the Initial Public Offering (IPO) route, aiming to raise **$256 million (€260 million)** by selling a maximum of 13,000,000 new shares to fuel its cybersecurity and digital technologies expansion.

Financial experts suggest these moves are just the beginning of a new era for the IT industry. "There was a 'big bang' moment in the market in Q1 this year when SoftBank, one of the most widely known venture capital firms in the world, discovered the intersection of cloud, distribution, MSPs, and marketplaces with its investment in Pax 8, suggests Panettieri. "The cloud is where a lot of transactions are happening, and SoftBank wanted in on that action, showing the value of these marketplaces and apps."

Over the past several years, distributors have been involved in mergers and acquisitions, PE and VC investments to first-time and additional rounds of public trading.

A Positive Forecast for IT Investments

Financial experts are optimistic about the funding outlook for technology companies, especially organizations that provide business-critical solutions. "We are seeing a lot of investment flowing to application and data-specific cybersecurity," adds Panettieri. "The value comes from protecting information wherever it resides, including in the cloud and multiple cloud applications like AWS and Azure. Private equity firms raised multiple billions of dollars in the second half of 2021 that they still have to spend in this market."

The question is whether those funds stay in banks or investment accounts, fuel business expansions, or drive M&A activities. Historical data may be one of the best predictors.

"Over the past couple of years, **we have seen a record amount of money invested by private investors such as venture capitalists and private equity investors,**" emphasizes Troy Cogburn, Director of Vation Intelligence with Vation Ventures. "Prominent venture capital firms such as Lightspeed Venture Partners, Battery Ventures, Andreessen Horowitz, and Tiger Global have all raised record amounts, and we can look to their theses to see where those investments will go. Global firms are still deploying this record capital within the enterprise, consumer, health, biotech, and fintech practices. More specifically, within enterprise IT, **firms are investing in infrastructure software, cloud, cybersecurity, data, AI, SaaS, developer tools, and solutions that impact the future of work.** I believe that we will continue to see the most growth in data, cloud, and cybersecurity areas, where there is a significant demand for new technology solutions from end customers."

Cogburn also expects those investors to continue targeting enterprise, consumer, health, biotech and fintech practices. More specifically, companies that develop and provide infrastructure software, cloud, cybersecurity, data, AI, SaaS, developer tools and 'the future of work' applications should be top prospects for PE and VC funds. He also points out a general sales growth trend in 2022, with **62% of companies expecting their IT budgets to increase** and 32% remaining at the same level as last year. Those companies are focusing their spending on emerging technology areas covering current top-of-mind solutions such as cybersecurity, cloud infrastructure, and business intelligence.

Potential Challenges

While investment in the IT industry is unquestionably strong today, will the current trends endure? Individual market predictions are a bit like betting on horse races. Past performance is definitely a large factor in predicting future results, but internal and external forces can significantly affect outcomes.

In the information technology space, business valuations can rise and fall quickly on the latest news or earnings reports. Like the technology field, some markets fare well in a recession or economic downturn, while others, like housing and automotive, see more elastic demand curves. IT companies that rely heavily on the more economically susceptible verticals may experience a drop in business valuation and struggle to find investors or M&A partners. A common best practice among technology executives is diversifying their customer base, allowing their teams to adjust sales and marketing activities to meet demand and preference shifts in each market. Flexible business creates more revenue opportunities, a major plus for potential investors.

Cogburn noted a potential slowdown in venture capital investment because of the uncertainty and volatility of the public market. "While the dollars are down this year, we are still ahead of pre-COVID investing. We also see late-stage high-growth startup valuations dropping from around 100 x ARR to 20 x ARR."

As a result of those changes, his team expects more investment in series A and B funds and the time between funding rounds to increase. "Rather than every nine months like the past two years, the time between deals may extend to 18 months."

"While the dollars are down this year, we are still ahead of pre-COVID investing."

– Troy Cogburn
Director of Vation Intelligence with Vation Ventures

The ability to scale sales and maximize various process efficiencies may factor into current and future valuations.

Can Distribution Affect IT Investment?

Good business partners can help organizations grow sales, profitability, and market share. Increasing any or all of those key metrics will help validate the long-term viability of a company while also raising its valuation and investment potential. A strong partner network makes it easier to scale the business with fewer headaches and cost concerns.

IT distributors provide that type of support daily, and vendors and ITSPs can leverage sales and marketing programs, marketplaces, solution design and development, and logistics support. Distributors expand the footprint of both communities and streamline processes to increase efficiencies and scalability. SaaS suppliers can quickly ramp up deployments and revenue with access to large communities of IT service providers and their collective clients. ITSPs can also leverage these relationships to cost-effectively scale their businesses using all the available and flexible resources.

While these key business relationships may not show on the corporate profit & loss statements, investors are sure to note the value of these alliances in the financial performance. Just as critically, the ability to scale sales and maximize various process efficiencies may factor into current and future valuations.

EDUCATE ◢ ADVOCATE ◢ INFLUENCE

Email info@gtdc.org | **Website** www.gtdc.org