

Seven Software M&A Takeaways for Life After COVID-19



CONTRIBUTORS

[Tom Burgett](#), Managing Director

[Will Bowmer](#), Managing Director

[Matt Cautero](#), Vice President

As technology investors consider where to be active amidst the COVID-19 crisis and the months that will hopefully follow later this year, we are increasingly being asked what “the market” will look for in new investments. Given the amount of scrutiny that we expect to be placed on business performance through and immediately following the C-19 crisis, we wanted to share thoughts around the business profile and attributes that will resonate most loudly with potential buyers as we eventually enter our “new normal.”

Observations and Recommendations of Crisis Period Business Actions and Performance

The seven items listed below can serve as loose guides to rally your teams around common goals that will not only serve you well through the crisis but will also provide future benefits as you position your business for a potential sale or capital event in the months post-crisis.

1. RECOGNIZE THE GROWING DISTINCTION BETWEEN “MUST-HAVE” AND “NICE-TO-HAVE” SOLUTIONS

As customers have instinctively frozen or severely tightened budgets in response to the crisis, we have already seen the early days/weeks of a slowdown in new software purchases. Solutions that drive business performance and have a discernible return-on-investment (“ROI”) are still able to close new business while others are struggling. An increased focus on ROI-driven messaging can accelerate sales velocity in an otherwise difficult selling environment. If not already a key element of your sales process, endeavor to quantify the critical elements of your value proposition, embed them into your sales and marketing materials and use your sales team to convey the message to your clients.

2. RENEW YOUR FOCUS ON CUSTOMER SUCCESS AND RETENTION

Customer retention and the resulting contribution to recurring revenue and cash flow are of utmost value to software businesses in any environment. In a crisis environment, protecting that cash-producing asset becomes absolutely critical. Not only does maintaining or improving retention protect immediate-term cash flow, but it also reinforces the must-have nature of a company’s product offering. A focus on increasing usage, rapidly responding to help inquiries and maintaining flexibility
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on contract and payment terms will accentuate the value of your solution and drive loyalty. As the crisis abates, investors will understand why new client acquisition will have slowed for a period, but your ability to maintain or improve client retention will demonstrate better than almost any other metric why your solution is essential to your clients.

3. MAXIMIZE THE VALUE OF YOUR EXISTING BASE

In a period when landing contracts with new clients is extremely challenging, the ability to cross-sell or upsell to an existing customer base that already trusts your business as a partner can offset shortfalls elsewhere. Happy customers that already know you and are actively using your solution can and should be much easier to sell additional functionality and/or additional users. While you may need to tread lightly to avoid the perception that you are overly aggressive, now is the time to nurture those relationships and be vigilant in recognizing and seizing opportunities to sell additional products or functionality. Along with gross client retention, your ability to demonstrate positive net retention metrics will validate a “land and expand” strategy and reinforce the “must-have” nature of your solution better than almost any other metric.

4. BE A PARTNER TO CLIENTS THROUGH THE CRISIS – IT WILL PAY DIVIDENDS LATER

A far-ranging group of providers have made their solutions available for free for a period to help both existing customers and prospects manage their businesses and/or serve their clients effectively through the challenges of quarantines and stay-at-home orders. Businesses that really deliver value to these “trial” customers, both through their products and their services, should convert a healthy percentage of those accounts to paid subscriptions in the next budget cycle. While used by many successful companies (e.g., Slack or Spotify) well before the C-19 crisis, this “product-led” strategy will demonstrate the power of your software and serve as a highly effective lead generation device at a time when your potential clients are struggling to justify additional expenditures.

5. MANAGE CASH CAREFULLY

As the old saying goes, get cash when you can, not when you need it – other strategies will be costly. Balance the need to take care of your customers with the need to preserve and manage your own cash needs and avoid having to go in search for cash at a time when it will cost more than it has in over a decade. Not only do you avoid problems during the crisis, but you will maintain greater strategic flexibility and more control over your future exit options post-crisis. Areas where you should be spending time include: conducting a thorough analysis of areas where you can reduce variable costs, carefully managing accounts receivable while remaining a partner to your customers, revisiting material capital expenditure plans and, if you are not profitable, your burn rate. Remember that, while valuable, future MRR and ARR cannot fund today’s payroll and operating expenditures.

6. UPGRADE YOUR TEAM AT ALL LEVELS

In a dislocated employment market, with unemployment numbers not seen in generations, senior leaders have a once-in-a-lifetime chance to find upgraded talent at almost all positions. Take advantage of the opportunity and position your business for even stronger performance as markets and economies reopen. Tap into the network that you have built as well as your broader ecosystem to find the candidates that are not only qualified, but who will be outstanding fits

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within your corporate culture. Avoid candidates looking for “any port in a storm,” and focus on long-term teammates that will help you create value in the months and years ahead.

7. TRACK CRISIS RESPONSE ACTIONS TO FACILITATE A FUTURE NARRATIVE

Investors will take a critical eye to the decisions and actions of management teams as their businesses entered and then navigated the C-19 crisis. Tracking specific actions taken and their eventual impact on revenue or costs will enable teams to later articulate their thought processes and how their decisions enabled the continued growth and stability of the business.

The “Right” Time to Enter the Market May Be Sooner Than You Think

The market will be increasingly focused on putting money to work as we exit crisis mode, and businesses that conform to the profile here will be highly sought after in a post-COVID-19 environment. Those that are prepared to move quickly once the economic engines are revving up and financing markets are again moving fluidly will have the advantage of being ready to sell a hard-to-find asset at a time when those assets will be most prized.

WHAT TO EXPECT POST-COVID-19

Much as we see pent-up demand for other products and services that have been unavailable for a lengthy period of time, we anticipate the dearth of M&A activity today will drive a substantial increase in demand for new investments. As a category, we continue to see software providers outperforming other sectors and much better positioned to weather the C-19 storm.

Moreover, we believe software businesses that perform well through the crisis period will be particularly well-positioned to access the market and will likely receive a premium as a result. Those that can clearly articulate their ability to perform, or even outperform, through the crisis period and line up well against key growth and retention metrics should strongly consider accessing the market as the crisis begins to abate.

While these metrics attempt to calculate and quantify business performance, what they really point to in our current environment is a management team’s ability to confront and quickly navigate unexpected circumstances. At the same time, they will reflect the importance of a product to its customer base and the level of loyalty created in that customer base through trusted relationships and consistently high levels of service.

*Similarly, businesses that experienced some softness in new business briefly but rebounded quickly will also be rewarded.

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