

Perspectives on the UK cybersecurity M&A landscape



SUMMER 2019

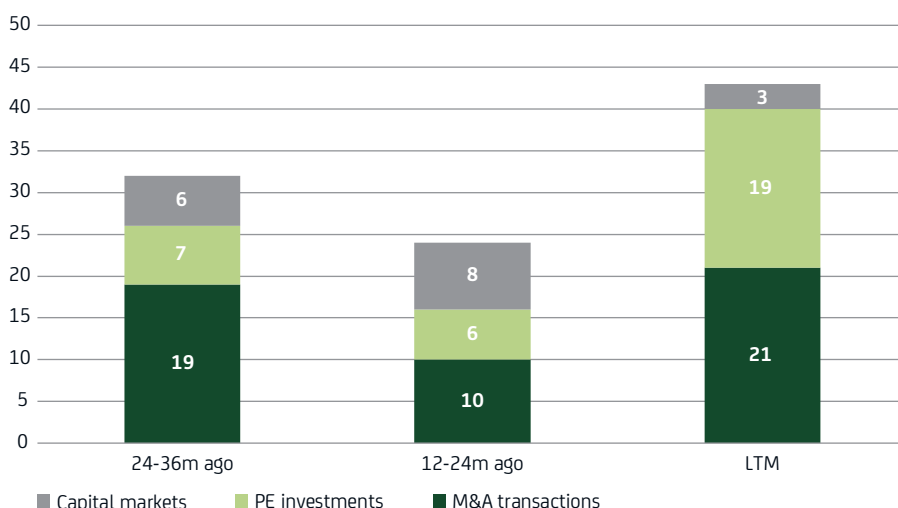
Investment in the UK cyber market has trebled in the last twelve months

In a sector report that we produced three years ago, we predicted that the UK cybersecurity market would attract investment, both from high-risk venture capital into fast-growing innovative start-ups and, increasingly, from mainstream private equity investors. In the report we highlighted three key observations:

1. M&A transactions, IPOs (initial public offering) and venture capital raisings in the cybersecurity space were at an all time high
2. Both private and public sectors were experiencing a large number of damaging, costly and high-profile data breaches
3. Today's UK start-ups would become tomorrow's established and successful mid-market businesses

A review of UK cybersecurity transaction volumes since then (see Figure 1, chart below) shows the increasing investment interest in this sub-sector, both from corporate acquirers and private equity investors.

Figure 1: Number of UK security and infrastructure software transactions



Source: Megabyte

Of course we expect to see some familiar names among the primary UK corporate acquirers, such as Mimecast and MicroFocus, and there will always be a high volume of venture capital investments in the smaller, innovative, high-growth businesses in the sector.

We are starting to see ever-greater mainstream private equity interest in cybersecurity businesses as the sector gradually matures. Examples of this include Tenzing's investment in Smoothwall and Livingbridge's investment in Adarma (formerly ECS Security). We are also aware of other high profile private equity houses that are currently courting various businesses in the space.



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A plethora of innovative UK cyber software businesses are emerging to disrupt the established vendors and keep pace with the threat landscape. Over the last 12 months, corporate M&A transactions more than doubled and private equity investments more than trebled. In 2020, we expect the sector to continue to be a hotbed for transactions, funded by investors and trade acquirers alike.

EMMET KEATING
DIRECTOR, TMT

Sector highlights

Key themes

Market themes

- ▶ A Q4 2017 survey showed that 43% of UK businesses (72% of large organisations) had experienced recent cyber breaches/attacks. CIOs/CTOs of corporates are generally receptive to approaches from innovative UK cyber businesses looking to market their latest solutions
- ▶ The European cybersecurity market is lagging behind the more mature US market, with significantly lower security software spend per GDP. The UK has the opportunity to lead cybersecurity innovation and development in Europe, and European corporates will have no choice but to invest to the levels of US counterparts to secure their enterprises
- ▶ Installing best-of-breed security software and outsourcing IT security management can ensure optimal security and deliver significant cost savings. While simplest in theory to procure all security solutions from a one-stop-shop provider, the demand for niche specialists solving specific technology problems remains very strong

Generating growth

- ▶ Cybersecurity is experiencing rapid growth in the UK (c.10% p.a.) driven by increasing awareness, growing threat levels and the recent issuance of GDPR. UK businesses can benefit from access to a broader range of financing options than ever, to invest to drive continued growth
- ▶ From an M&A perspective, security specialists are looking to either broaden their technology offering or geographic reach through targeted acquisitions. Shareholders and investors recognise the opportunity to accelerate revenue growth and enhance technology capabilities through executing a buy-and-build strategy. There are plenty of small innovative businesses for consolidators to target

Transaction highlights

Date	Investor	Target	Type	Value	Sales Growth	Target description
Jun-19	Livingbridge	Adarma	Buy-out	n/d	n/d	Enterprise-level managed security services provider
Jun-19	Accel Partners	Privitar	VC funding	£30m	n/d	User data privacy and protection software
Apr-19	SoftBank Capital	Onfido	VC funding	£38m	+340%	AI-powered identity verification solution provider
Feb-19	Sequoia Capital	Tessian	VC funding	£32m	+300%	Machine learning led email security platform
Nov-18	Accenture	Quantexa	Strategic investment	£100m	n/d	Anti-fraud data analytics software business
Oct-18	Dawn Capital	Garrison Technology	VC funding	£23m	n/d	Secure web gateway solutions
Jul-18	Bomgar	Avetco	Acquisition	£200m	+51%	Endpoint security solutions and Windows privilege management software solutions
Jun-18	Balderton Capital	Tessian	VC funding	\$13m	+500%	Email security and data integrity solutions
Jun-18	F-Secure	MWR InfoSecurity	Acquisition	£80m	+28%	Cyber research/consulting services business offering phishing protection and cyber attack detection
Mar-18	Turn/River Capital	Netsparker	Capital raise	\$40m	n/d	Web application security scanning software
Oct-17	Tenzing	Smoothwall	Buy-out	£50m	+15%	Specialist developer of innovative web filtering and safeguarding solutions used in the public and private sector
Sep-17	Octopus Ventures	Digital Shadows	VC funding	\$26m	+50%	Cybersecurity threat identification analytics provider

CASE STUDY: MBO OF ADARMA backed by Livingbridge

Founded in 2009, Adarma (formerly ECS Security) provides a range of cybersecurity consultancy, assurance and managed security services to FTSE 100 and FTSE 250 enterprises in the UK. Analytics and automation are at the core of these services, with strategic technology partners including Splunk and ServiceNow.

Having spent time with the business preparing for sale, a streamlined sales process was executed involving selected technology specialist private equity investors.

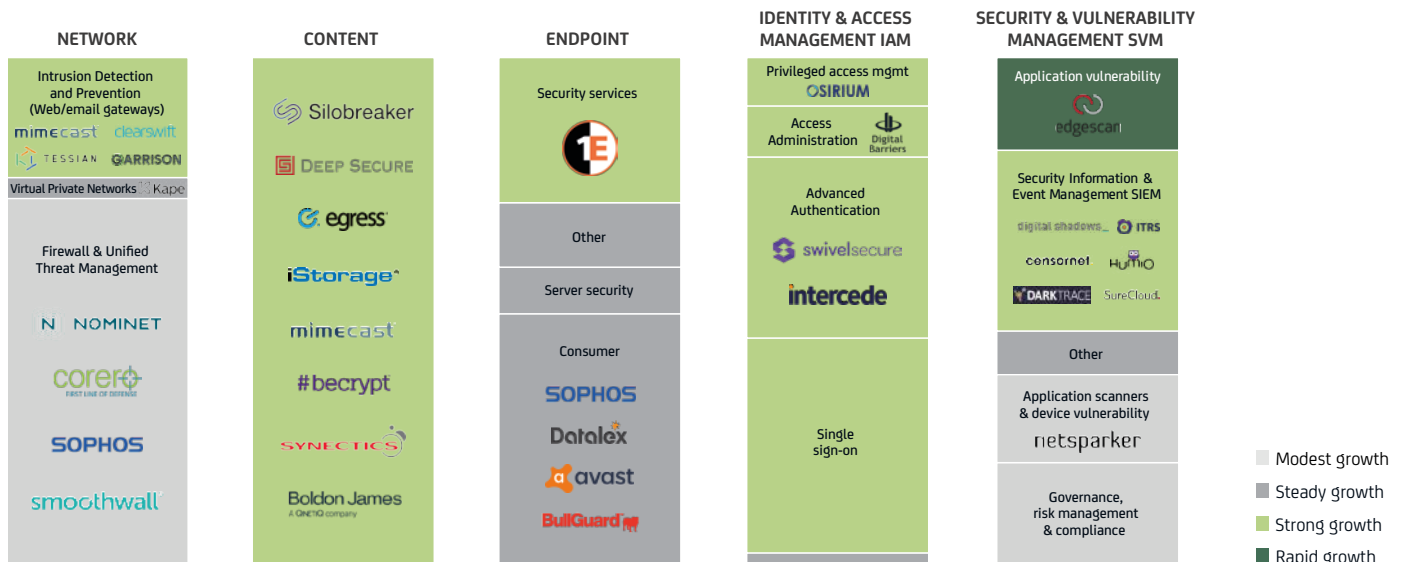
Livingbridge consistently demonstrated its appetite and commitment to acquiring the business, and delivered an attractive deal for both the exiting shareholders and MBO team.

The transaction creates the largest independently owned security services business in the UK, with clear potential to rapidly scale further with its new investors on board.

Market growth map

Certain sub-segments of the market are experiencing rapid growth with others demonstrating steady, albeit still very healthy annual growth. Our data indicates that the UK cybersecurity sector, as a whole, is growing in the region of 10% per annum.

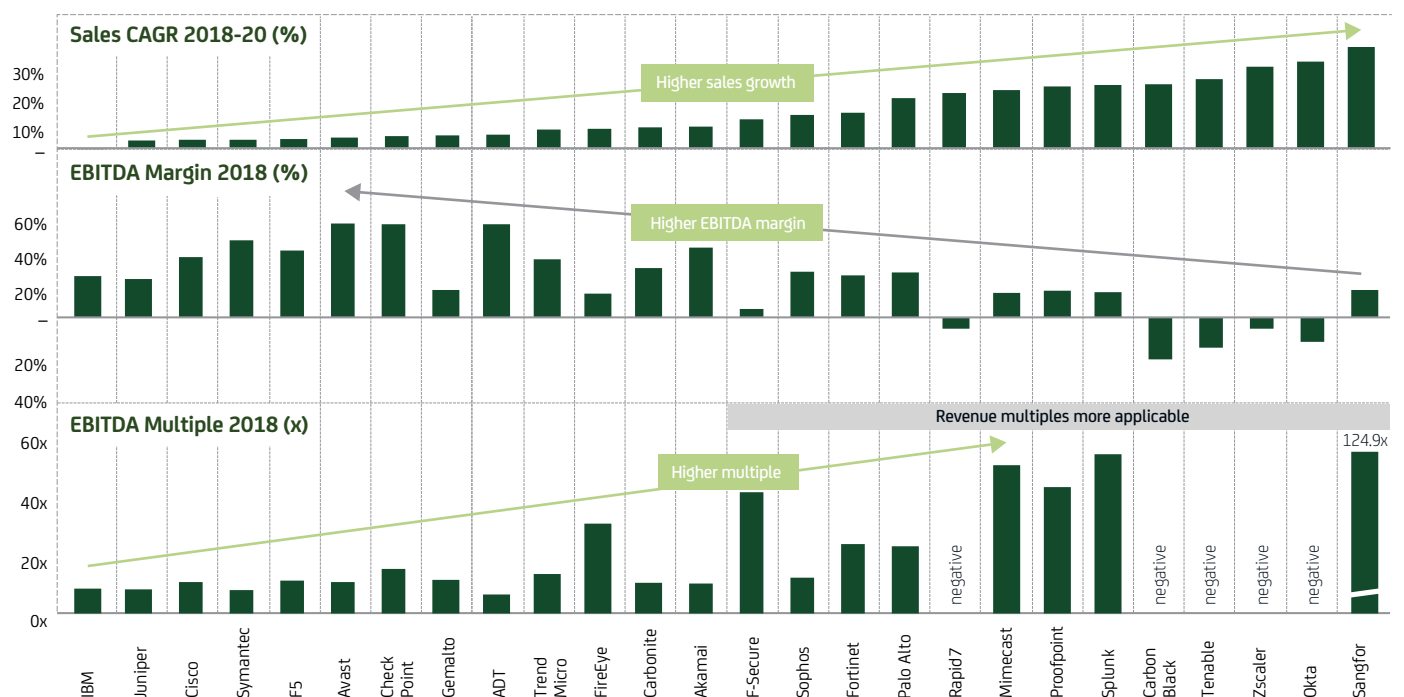
The following UK cybersecurity market heat map indicates the relative growth prospects for different sub-segments in the market, as well as some of the promising UK businesses in the sector:








Valuation analysis

Some high-growth businesses are transforming dramatically and some of the valuations are correspondingly high. These businesses tend to have annual revenue growth of 20% or more (sometimes significantly more) and are often valued based on a multiple of revenue. Most of these businesses invest some of their earnings to drive continued rapid growth, and profit is not the stakeholders' primary concern.

Other businesses have a different strategic outlook – providing robust, secure solutions with greater focus on profit generation. While these businesses tend to be growing more slowly, they are often highly embedded with their customers and delivering high profit margins and reliable annual cash flows. These businesses tend to be valued based on a multiple of the sustainable annual earnings, a more commonly seen valuation approach across all industries.



Selected cybersecurity credentials

  ADARMA  formerly  MBO  LIVINGBRIDGE	  CNS GROUP  SALE  Six Degrees	   INVESTMENT  MML <small>RETURN ON IDEAS</small>
   TROPO SALE  CISCO	   Nakina Systems SALE NOKIA	  Fixmo SALE  Good

Alantra UK senior TMT team

Our advice covers company acquisitions and sales, management buy-outs and buy-ins and raising equity, growth and debt capital from both public and private markets.



Emmet Keating
Director

emmet.keating@alantra.com
+44 (0) 121 654 5000



James Chapman-Andrews
Partner, Head of UK TMT

james.chapman-andrews@alantra.com
+44 (0) 20 7246 0500



Richard Sanders
Partner

richard.sanders@alantra.com
+44 (0) 121 654 5000



Paul Vanstone
Director

paul.vanstone@alantra.com
+44 (0) 20 7246 0500

ALANTRA

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