



Building a better working world

COVID-19: Technology sector perspectives



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Technology is at the forefront of industries going through dynamic change due to the COVID-19 pandemic. It presents risk and opportunities that are unique to each company in the sector.

The COVID-19 pandemic has revealed the extent to which we rely on technology and how it has become integrated with almost every facet of our economy and life. We have seen technology applied to keep “business as usual”, to replace normal social interactions and to be mobilized for good to fight the COVID-19 pandemic. Despite that, the discussion around the economic impact technology companies are facing is much more nuanced. Technology is a broad sector and no technology company is being impacted in the same way. By looking at the specific characteristics of technology companies, some consistent trends can be found.

Impact by subsector

Generally, software was impacted less directly than other subsectors, as it did not experience supply chain issues that burdened other subsectors, such as IT procurement. There are a number of applications that will experience tailwinds as the current situation increases dependency on the technology.

- ▶ Communication and collaboration solutions are experiencing a significant uptick both as a way for employees to connect and as a replacement for social interaction. These companies have seen a dramatic increase in users, which has presented an opportunity for historic levels of growth, but also exposed issues with infrastructure and security. Verizon’s acquisition of BlueJeans indicates the appetite from communication service providers to move upstream amidst the transition to 5G to better service enterprise customers, although the deal has implications beyond the current remote work requirements.
- ▶ Security solutions are being re-evaluated by many companies as there is a mass migration of the workforce to a remote set-up. Being able to secure confidential information is crucially important for companies seeing remote work as a viable solution in the long term. Services being evaluated include, but are not limited to, data protection, secure back-up, and document retention and compliance.

- ▶ Providers of digital experience, such as streaming and gaming companies also have the potential to grow as people look for new ways for entertainment and social interaction, representing a unique opportunity for these companies to engage new users. Almost all gaming and gaming tech companies we have spoken to have seen some of their best financial and game metrics over the last few weeks.
- ▶ Cloud technologies are essential for many companies to operate remotely and engage with customers and employees. Cloud technologies are expected to play a pivotal role in enabling sales teams to engage with clients virtually and for development and delivery teams to create and implement solutions through remote interfaces and increased automation.
- ▶ Contactless payments have seen increased adoption as new awareness around hygiene has led people to re-evaluate the use of cash and other payment technologies that are constantly touched by others. Card issuers have already put more than 300 million cards into the US market alone with contactless capabilities.

Impact by end-user industry

While the actual subsector of operation may be the best indicator of COVID-19 impact, the end-user industry of technology customers can be equally important during this time. Some technology companies are essential to the operation of industries that are seeing significant demand right now, while other technology is being impacted by end-user industries being hard hit by the economy.

- ▶ There is high demand for industries such as health care, logistics, transportation and consumer staples. These industries are either at the forefront of the COVID-19 pandemic or are seeing demand as a result of self-isolation measures. Technology companies that either provide a solution to these industries or have a higher concentration of these end-user industries are expected to benefit from that demand.

- ▶ Meanwhile, sectors like hospitality, retail and energy have seen a significant decline in demand as people are travelling less and saving more. Technology companies with too much reliance on these sectors could be exposed to significant risk, especially if they provide a discretionary offering or are priced at a premium to competitors.

SaaS companies have seen relatively modest declines so far. However, the recurring nature of these businesses does not insulate them from the impact on the sectors they serve. Several of our SaaS clients are evaluating deferred payment plans, pricing discounts or stretched receivables. Now more than ever, businesses with a focus on customer service have shone through. As retention has trumped acquisition in the last few weeks, these businesses have shown more resilience in some cases than their previously faster-growing peers.

What this means now and going forward

It is likely that much of the impact we are seeing now can be considered a “first wave” that will have a sharp impact on technology companies, but in many cases will subside over time. Many of the impacts cited related to end-user and subsector are specific to demand directly from the existence of the pandemic, like the impact on healthcare, or the consequent self-isolation measures. While companies may have less control over these initial consequences, they can begin to best position themselves for the future.

After the pandemic has decreased its burden on the healthcare system and self-isolation measures have loosened, companies will need to begin to understand how COVID-19 will impact them going forward. For example, this period of high adoption for collaboration tools and digital entertainment may create a wider base of users going forward and new perspectives on hygiene may create long-term preference towards contactless solutions. Companies need to be thinking of short-term impacts during this first wave and the longer-term implications as some of the lessons from this pandemic become engrained in consumer preferences and spending.

The impact on M&A and Capital Markets as it relates to the technology sector is only beginning to be seen, but some trends are starting to emerge at this time.

Thoughts on Technology Sector M&A and Capital Markets

- ▶ Technology M&A processes are not immune to the crisis and there have been pauses and delays in deals and IPO plans. Companies, especially those with near-term operational and financial challenges, are expected to see pressure on valuation and changes to deal structure to include more contingent payouts.
- ▶ Companies will continue to evaluate opportunities for diversification, which may mean pivoting from serving only small and medium businesses or being concentrated in a single vertical.
- ▶ Companies in non-tech sectors that do not have any internal technology capabilities or assets may be looking to build their own technology infrastructures to help diversify their business or de-risk their reliance on their technology vendors.
- ▶ Investors remain interested in technology companies during this time and many have dry powder to deploy on attractive targets, however, any deal evaluation will be clouded by the difficulty in estimating run rate revenue / EBITDA.
- ▶ Companies looking to pivot their offering to best position themselves for the future will need to evaluate their capital structure and financing capacity at this time in order to pursue opportunities that may present themselves.

Conclusion

Technology will continue to play a major role in the COVID-19 pandemic. Each organization will be impacted differently based on a number of factors. This situation could play out for technology broadly in two waves: the current, more significant wave, that has direct consequences due to the pandemic and self-isolation measures, and a future change in the way consumers and companies interact with technology. M&A would be an important tool to help navigate the situation now and going forward.

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