



# The MSP M&A Market View for 2023

January 2023

Confidential



**The MSP Market Continues to see Consolidation Going Into 2023.**

451 Research's M&A Knowledgebase

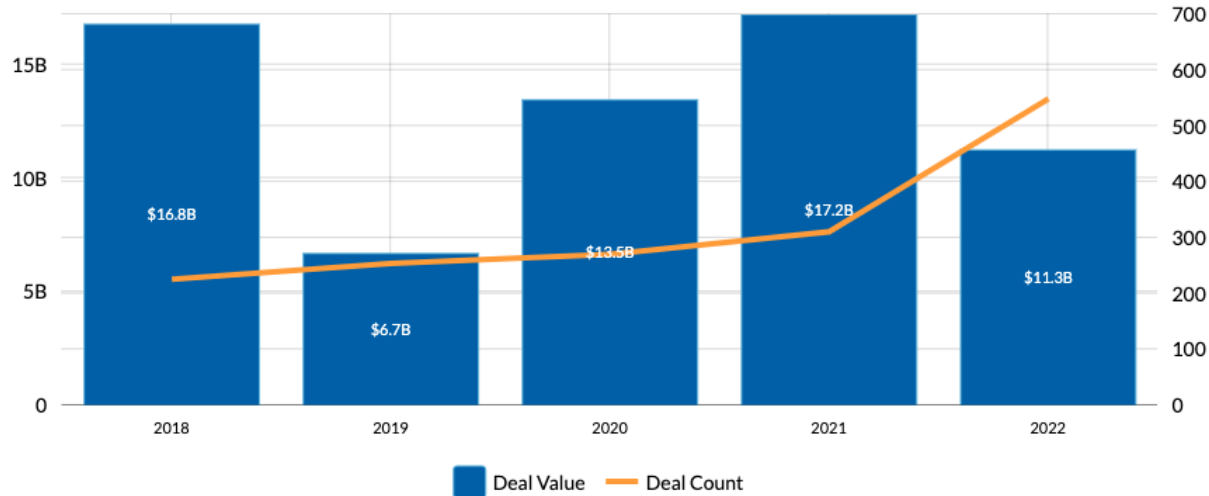


## Accelerated Consolidation

M&A transactions in the Managed IT Service Provider (MSP) market saw a significant increase in total deal volume in 2022:

- There were 549 transactions here in 2022, up over 75% from 2021's 311 transactions
- Total Value in 2022 however, decreased from \$17.3B in 2021 to \$11.3B in 2022 as buyers inked fewer blockbuster transactions during the year

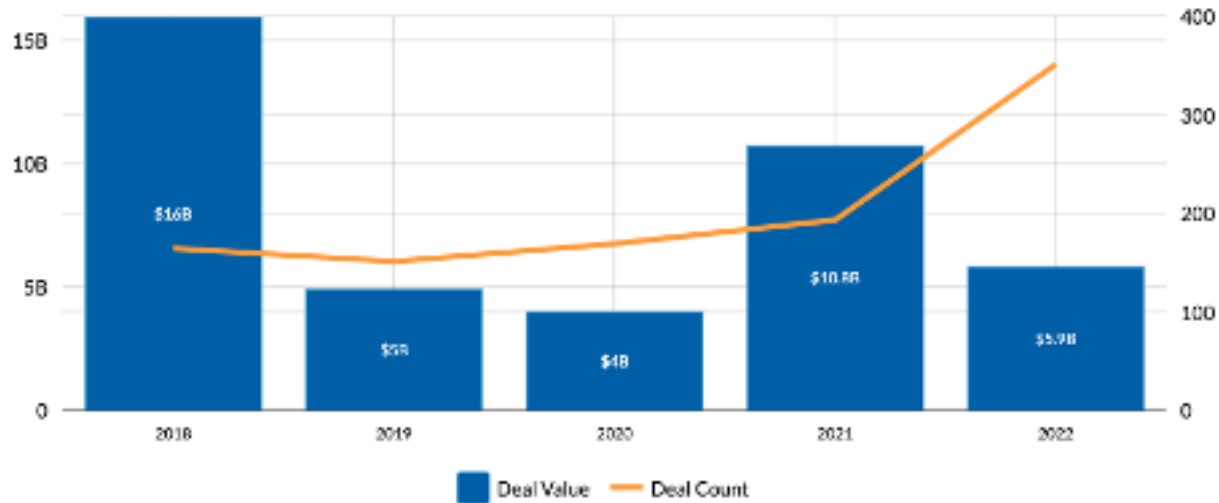
## Trends in the MSP M&A Market (Annual)



Looking at the underlying data, strategics still dominate the volume of M&A in this market, with 64% of the total M&A transactions in 2022. However, PE firms contributed just under half of the total valuation in 2022, a result of fewer, but larger transactions than strategic buyers.

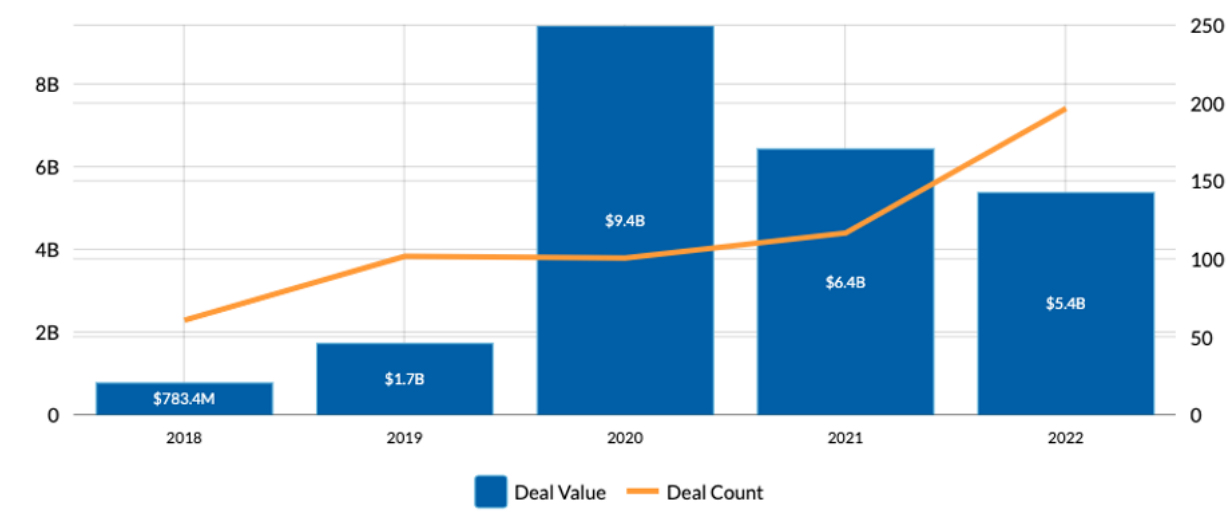
Note that in 2018, there were 5 transactions totalling \$15.9B, making up 95% of the combined value for the year – 4 of these deals were by strategic acquirers.

## Deals by Strategic Buyers in the MSP Market 2018-2022



Strategic buyers (growth-focused companies that are in, or adjacent to, this market – these can be public, private, or PE-backed) made up 64% of the total acquisitions announced in 2022 and just over half the total valuation. This would imply that strategic buyers were more focused on smaller transactions in 2022 than PE buyers.

## Deals by Private Equity in the MSP Market 2018-2022



Private Equity firms made up 197 of the 549 transactions in 2022 – 36% of the total but they contributed almost half of the total valuation in 2022. Interest snowballed by PE firms in this sector starting in 2020, but there was a significant jump from 2021 to 2022 by PE buyers.



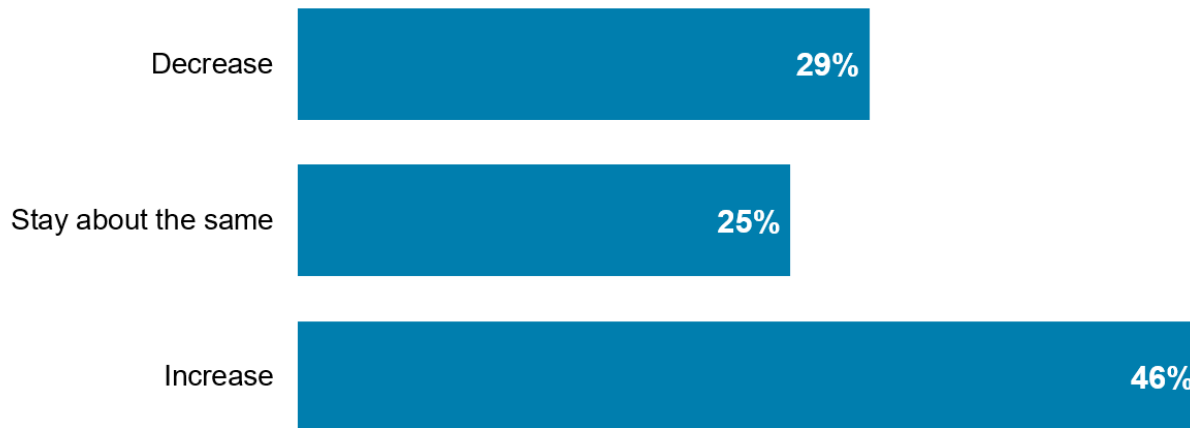
## 2023 Outlook:

- We foresee continued interest in this market in 2023 as buyers of all stripes see the opportunity in what is still a fairly fragmented market with many regional players. Strategics (these include the larger MSPs who are now often backed by private equity investors) continue to plug technology gaps, increase market share, enter new geographies, and expand their teams through strategic acquisition. There are now several private equity firms active in this market, as well as many regional and national MSPs, seeking to accelerate their growth and remain competitive through non-organic growth.
- Buyers view strategic acquisitions in the IT, Managed, and Professional Services market as a key part of continued market expansion and growth, and are likely to continue to focus on additional acquisitions this year.
- A study released by EY this month revealed ***that the biggest opportunity for tech companies in 2023 is to adopt an active M&A strategy***. The study found that 72% of tech CEO respondents plan to pursue M&A in the next 12 months, compared with 59 per cent of CEO respondents across all industries.
- The sheer volume of buyers seeking acquisitions will help to keep competition brisk and valuations steady, even in the face of global economic and socio-political upheaval.



## > 70% of Companies Actively Acquiring in 2023

In 451 Research's latest survey released in December 2022, respondents shared they were looking to get back to dealing in a market that has recently been humming along at a historically elevated rate of about a half-trillion dollars of spending each year (all Tech M&A globally).







## What are Buyer's Looking for?

Buyers are becoming laser-like in their focus on finding the right strategic acquisition targets. For many, the following attributes are key:

- Recurring revenue under agreement as a percentage of total revenue – most are looking for >60% recurring.
- In addition to the amount of recurring revenue, buyers will quickly want to determine the quality of the recurring revenue: is it primarily labor-driven? Or is it generated as a function of the systems the MSP is using to monitor their clients? The former is more costly to scale, making the latter of greater interest.
- It's important that you have no revenue concentration among a small group of customers.
- EBITDA of \$500k to \$2m is seen as “add-on” potential while EBITDA over \$2m is viewed as a potential platform acquisition or investment by many.
- The size of a company is also important, with many buyers interested in MSPs that are over \$10m in revenue.
- Smaller firms are less accretive and generally need more investment to build out their teams and internal systems.



## What are Buyer's Looking for?

- Specializations in vertical markets such as Law firms can be important.
- What size customers does the company service? Many buyers like enterprise customers, but there are firms that specialize in the SME market and are looking for this.
- Gross margins and net operating income will be scrutinized very closely, especially now as we move into a less predictable economy. It's important to ensure you are capturing Cost of Sales correctly to reflect your firm's true Gross Margin – this shows a buyer how efficiently the company is utilizing resources.
- In some cases, it's necessary to “right-size” salaries and benefits to be more in-line with market.
- These adjustments might come at the expense of valuation.
- Location of the MSP – many buyers are looking to cover key areas on both coasts and in the Midwest as they grow out national coverage.



## What are Buyer's Looking for?

- Customer satisfaction scores (CSAT), Net Promoter scores (NPS\*), and customer churn and retention are extremely important, particularly in today's economy where it can be easier to drive additional revenue from existing customers than it is to sign new ones
- Average number of tickets and response times.
- Employee certifications and retention – how strong is the team?
- NPS Scores from 0 to 6 count as detractors, while 7 to 8 is neutral, and respondents selecting 9 or 10 are your promoters. Subtract your percentage of detractors from your percentage of promoters to determine your NPS.



## MSP Growth and Profitability

### *The Most Profitable MSPs are Also the Fastest Growers*

According to Service Leadership, MSPs in the top quarter of the market for profitability grew their total revenue, and recurring revenue the fastest. This is important for MSPs to note, as many firms that are investing in growth are apt to give themselves a “pass” for lower profitability. Market research shows this just isn’t the case.

The bottom quarter of the MSP market for profitability reports slower revenue and recurring revenue growth. This quartile also reported a lot of customer churn whereas the top quartile reported about 20% churn.

#### **To be in the top quartile, MSPs had:**

- EBITDA > 18%
- Total Revenue Growth >13%,
- Recurring Revenue Growth > 16%

#### **In the Median group, MSPs had:**

- EBITDA > 9%
- Total Revenue Growth >12%,
- Recurring Revenue Growth > 14%

#### **The lowest quartile reported:**

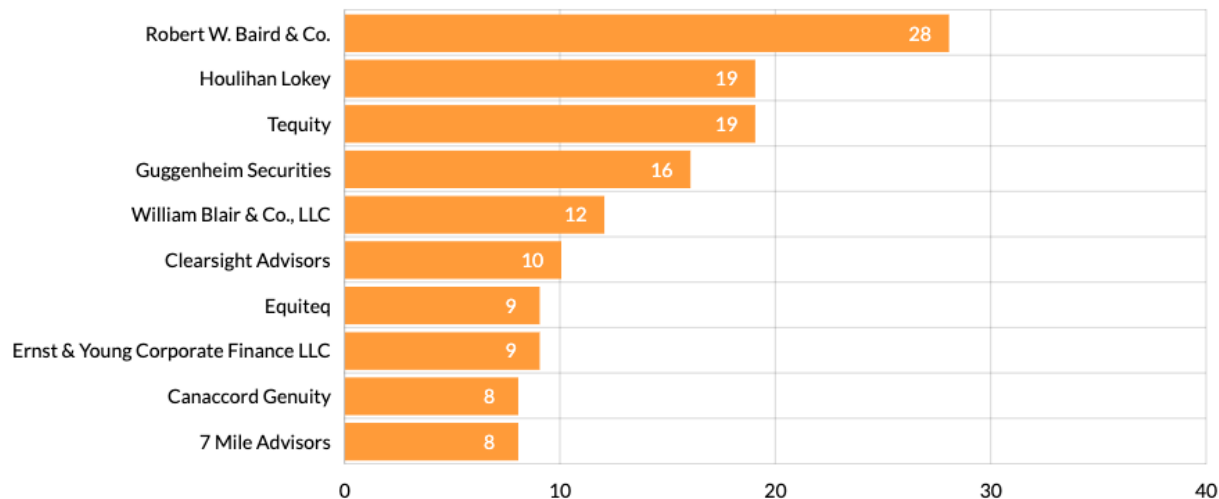
- EBITDA = < -0.8%
- Total Revenue Growth 4.5%, \
- Recurring Revenue Growth < -0.7%



## Summary

### Tequity is a Leading Firm in the Managed and IT Services M&A Market

If you have been contemplating acquisition to accelerate your growth, we can provide additional information on timing, preparation, metrics, and valuations.





# THANK YOU



88 Queens Quay West, Suite 2500, Toronto, ON M5J0B8



[info@tequityadvisors.com](mailto:info@tequityadvisors.com)

Diane Horton, CBI, CM&AA  
Managing Partner



416-993-1734



[dhorton@tequityadvisors.com](mailto:dhorton@tequityadvisors.com)