VENTUREDEAL M&A ANALYSIS

Research and opinion on recent M&A transactions.

Paychex Acquires Oasis Outsourcing

PTC Acquires Frustum For AI Generative Design Tech

iHeartMedia To Acquire Jelli For Programmatic Ad Buying Platform

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VentureDeal

Paychex To Acquire Oasis Outsourcing For PEO Business

Quick Take

Paychex (PAYX) announced it has agreed to acquire Oasis Outsourcing for $1.2 billion.

Oasis Outsourcing operates as a professional employer organization [PEO] to enable companies to outsource various human capital services.

PAYX is acquiring the largest privately-held PEO firm in the U.S. and stands to generate revenue and cost synergies as the PEO industry expands in the aftermath of the financial crisis.

Target Company

West Palm Beach, Florida-based Oasis Outsourcing was founded in 1996 to provide outsourced HR services, such as administration and development, employee benefits management, payroll administration, risk management, as well as staffing and recruitment services.

Management is headed by President and CEO Mark Perlberg, who has been with the firm since 2003 and was previously President and COO at PRGX.

Oasis' primary offerings include:

- Human Resources
- Employee Benefits
- Payroll Administration
- Risk Management

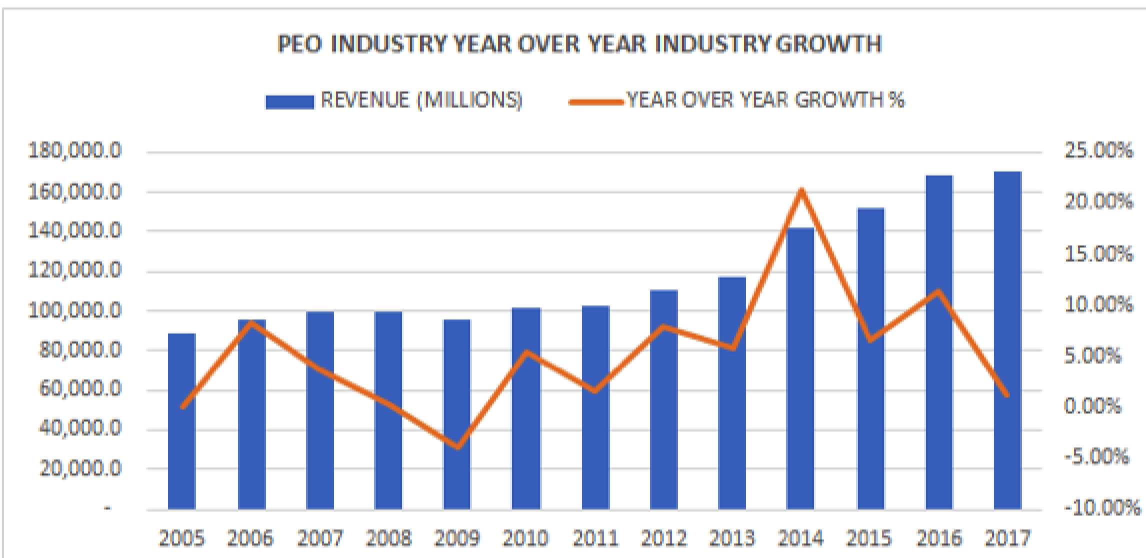
Company partners span the categories of insurance providers, accountancy, and financial partners.

Investors in the company include Stone Point Capital and Kelso & Company.

Market & Competition

According to a market research report by IBIS World, PEO (Professional Employer Organization) gross revenue for 2017 was $170.4 billion and is projected to grow to $177.7 billion in 2023. The PEO industry turned in $1.7 billion in profits for 2017.

This represents a CAGR of 9% between 2012 and 2017 and a CAGR of 0.7% between 2018 and 2023.



Year over year growth in dollars and percentage for the PEO industry.

Major competitive vendors that provide PEO services include:

- ADP Totalsource (ADP)
- TriNet (TNET)
- Insperity (NSP)
- CoAdvantage
- Barrett Business Services (BBSI)

Acquisition Terms and Rationale

Paychex disclosed the acquisition price as $1.2 billion in an all-cash transaction.

PAYX will pay for the deal 'through a combination of cash on Paychex's balance sheet and borrowings under existing credit facilities or new debt.'

Management expects to 'see a number of revenue and cost synergies as a result of this transaction,' although didn't provide further details about those synergies. Furthermore, the acquisition is expected to have 'minimal impact on fiscal year 2019 earnings per share.' Additional information will be provided during management's second-quarter earnings call on December 19, 2018.

A review of the firm's most recent 10-filing indicates that as of August 31, 2018, PAYX had $440 million in cash and equivalents and $870 million in total liabilities, excluding client fund obligations.

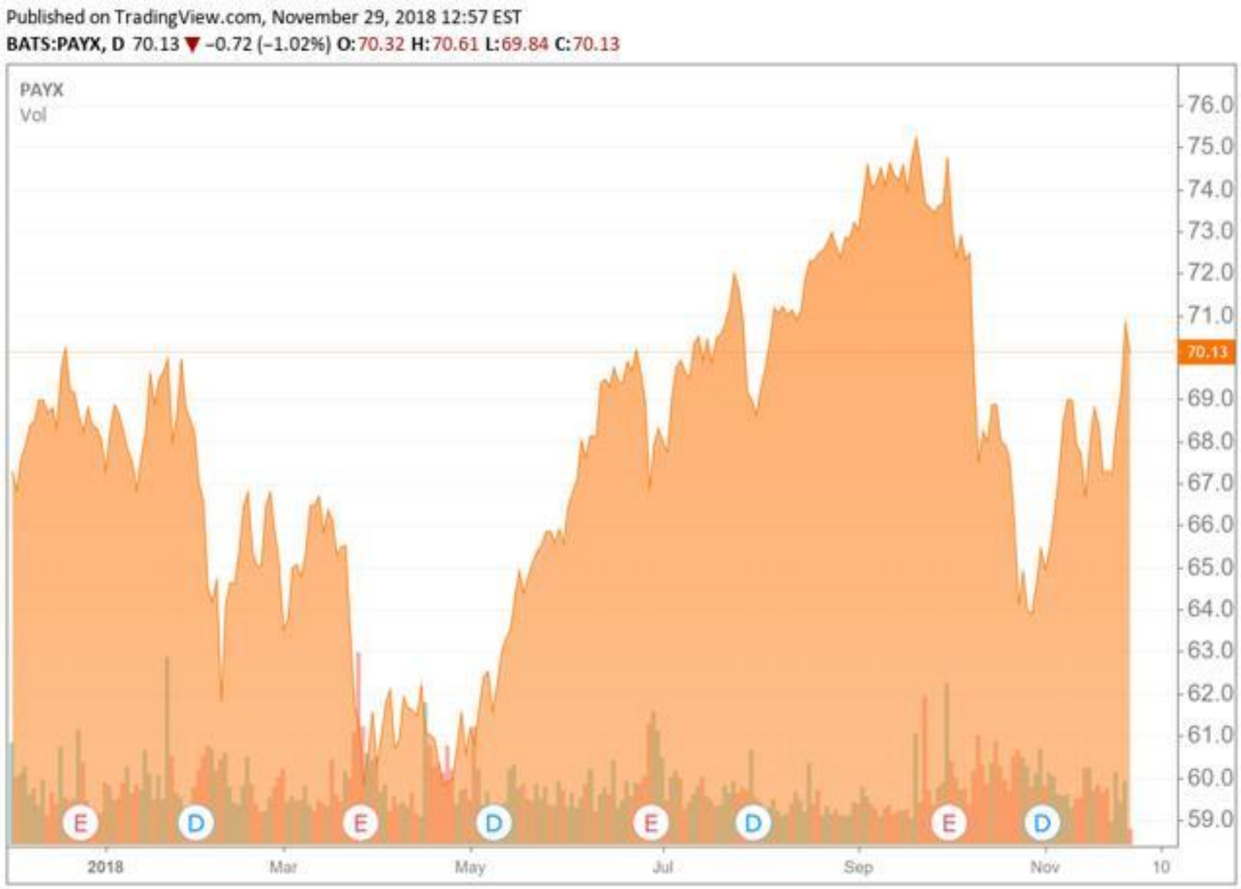
Free cash flow during the three months ended August 31, 2018, was $249.3 million, so it appears the firm has the cash flow to service the additional debt required to close the deal.

Paychex is acquiring Oasis to combine its payroll administration capabilities with the U.S.' largest privately owned PEO in Oasis.

As Martin Mucci, president and CEO of Paychex said in the deal announcement,

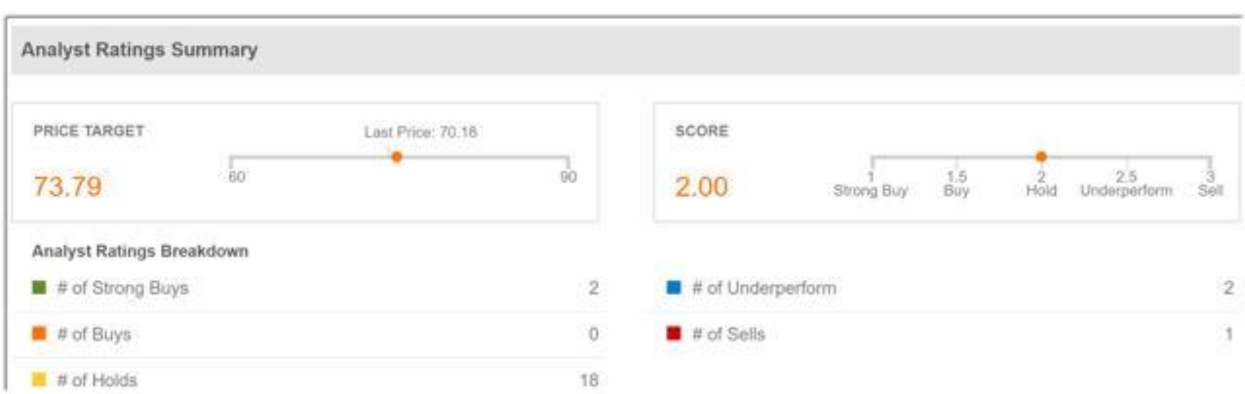
We know there's a growing need today among small and mid-sized businesses for HR technology and outsourcing services, especially given the ever-increasing number of regulations around issues like paid family leave, health care, and anti-harassment training requirements. Those businesses need the integrated technology and expert support Paychex (PAYX) offers, expertise that grows with the addition of Oasis. This acquisition will strengthen our PEO growth strategy, gain scale for new products with our insurance carrier partners, provide a new client base to offer Paychex retirement and time and attendance products, and augment our experienced management team.

In the past 12 months, PAYX's stock price has risen *4.2%* vs. the S&P 500 Index' rise of *2.1%*, as the chart below indicates:



Source: [Seeking Alpha]

Analysts believe that the PAYX stock is largely fully valued, based on their consensus estimates of around $74 vs. the current price of $70. Additionally, the vast majority of analysts have a 'Hold' rating on the stock, as the graphic shows below:



Source: [Seeking Alpha]

So, while I like the acquisition for the potential for revenue cross-selling and cost synergies, management has been tight-lipped about the benefits of the deal as well as the composition of assets it will use to acquire Oasis.

The stock has risen 5% since the deal announcement, although the overall stock market has been up which may account for some of the recent rise.

In any event, the PEO industry has shown remarkable top-line growth, especially in the aftermath of the financial crisis of 2008 - 2009.

From a strategic viewpoint, the combination appears to make sense on paper, combining the complementary capabilities of the two firms to provide small and medium-sized companies with a full suite of outsourced human capital and related administration services.

PTC Acquires Frustum For AI Generative Design Tech

Quick Take

PTC (PTC) announced it has acquired Frustum for $70 million in cash.

Frustum has developed AI-powered generative product design technology.

PTC has made an excellent strategic purchase to enhance its Creo portfolio of capabilities to help customers drive further design cost efficiencies and improvements.

Target Company

Boulder, Colorado-based Frustum was founded in 2014 to develop desktop and cloud-based Computer-aided Design [CAD] software that leverages AI to guide and inform the discovery and development of product designs.

Management is headed by Founder and CEO Jesse Coors-Blankenship, who was previously Senior Optimization Engineer at Autodesk.

Investors have invested at least $8.7 million in the company and include Next47 and H&S Capital Group. *Source: Crunchbase*

Market & Competition

According to a market research report by Prescient Strategic Intelligence, the CAD software market was valued at $8.3 billion in 2017 and is projected to reach $12.1 billion by 2023.

This represents a CAGR of 6.6% between 2018 and 2023.

The main drivers for this expected growth are the rising demand for precise designing and complex structure prototyping, advancements in technology, and increasing demand for CAD software in automotive, packaging, and medical verticals.

The solid models market is projected to witness the fastest CAGR, at 7.4%, during the forecast period.

Major competitive vendors that provide CAD software solutions include:

- Autodesk (ADSK)
- Bentley Systems
- Dassault Systemes (OTCPK:DASTY)
- GStarsoft
- Hexagon (HEX.OL)

Acquisition Terms and Rationale

PTC disclosed the acquisition price as approximately $70 million in cash and said in an 8-K filing that it drew on its credit facility to pay for the deal.

Management also stated that the deal would not 'add material revenue for 2019 or to be dilutive to the financial guidance PTC provided on Oct. 24, 2018.'

A review of the firm's most recent 10-K filing indicates that as of September 30, 2018, it had $285.8 million in cash, equivalents, and short-term marketable securities. Liabilities totaled $1.45 billion, of which long-term debt was $643.3 million.

Free cash flow during the 12 months ended September 30, 2018, was $211.8 million, so it appears the firm has ample resources for the transaction without undue financial hardship.

PTC acquired Frustum to expand its CAD ‘Creo’ portfolio of capabilities with its AI-enabled generative design system.

Generative design allows the engineer to enter design goals and constraints and the system generates potentially thousands of designs, running analyses on each one and enabling the engineer to iterate and select the more relevant designs.

As Jim Heppelmann, president and CEO of PTC stated in the deal announcement,

PTC is pushing the boundaries of innovation with this acquisition. Creo is core to PTC’s overall strategy, and the embedded capabilities from ANSYS and, later, Frustum will elevate Creo to a leading position in the world of design and simulation. With breakthrough new technologies such as AR/VR, high-performance computing, IoT, AI, and additive manufacturing entering the picture, the CAD industry is going through a renaissance period, and PTC is committed to leading the way.

In the past 12 months, PTC’s stock price has risen *40.5%* vs. the S&P 500 Index *2.1%*, as the chart below indicates:

Source: [Seeking Alpha]

Analysts are largely bullish on PTC's stock price, with a consensus price target of nearly $104 vs. the current price of around $89, as the summary shows below:

Source: [Seeking Alpha]

The acquisition of Frustum was likely valued on a 'team and technology' basis, rather than a revenue or EBITDA multiple since management stated that the deal 'would not add material revenue to 2019.'

Also, buying an already-developed solution will enable faster go-to-market response to demand for generative design capabilities that PTC has no doubt been encountering.

By combining Frustum's AI generative design system with its Creo platform, PTC can offer its clients and prospects the added benefits of further cost efficiencies due to the fast-iterative process since computing power is relatively low-cost when compared to high-priced engineers and the need for rapid response to market demands.

So, I view the deal as a strategic no-brainer for PTC's offering set. Investors should be cheered by management's nimble approach to the continually increasing client requirements for design efficiencies.

iHeartMedia To Acquire Jelli For Programmatic Ad Buying Platform

Quick Take

iHeartMedia (OTCPK:IHRTQ) announced it has agreed to acquire Jelli for an undisclosed amount.

Jelli provides programmatic buying and selling of broadcast radio services.

Although iHeartMedia received investment interest earlier in 2018 from Liberty Media (FWONA) and private equity firm Silver Lake, interested investors will need to exercise patience while we learn how the firm will emerge from Chapter 11 bankruptcy.

Target Company

San Mateo, California-based Jelli was founded in 2009 to develop a Web-based technology platform that enables advertisers and publishers to buy and sell audio advertisements programmatically.

Management is headed by Co-Founder and CEO Michael Dougherty, who was previously VP Business Development and Strategy at Tellme Networks.

Jelli's primary offerings are SpotPlan and RadioSpot.

Company partners or major customers include:

- COX Media Group
- Alpha Media
- Beasley Media Group

Investors in the company include First Round Capital, Relay Ventures, iHeartMedia, Universal Music Group, Intel Capital and Battery Ventures. *Source: VentureDeal Venture Capital Database*

According to a market research report by eMarketer, the digital audio advertising market in the U.S. reached $1.6 billion in 2017, growing from $1.1 billion in 2016.

However, the report also forecasts that total radio advertising spending in 2018 will be flat at $14.41 billion.

One major competitor that Jelli faces is Google (GOOG), which the report stated its 'demand-side platform [DSP] began accessing the inventory of several audio streaming services' in May 2018.

Acquisition Terms and Rationale

iHeartMedia didn't disclose the acquisition price or terms, didn't file an 8-K, and didn't provide a change in financial guidance, so the acquisition will likely be for a non-material amount.

A review of the firm's most recent 10-Q filing indicates that as of September 30, 2018, the firm had $311.2 million in cash and $7.3 billion in total liabilities, of which $5.3 billion was long-term debt.

Free cash flow during the nine months ended September 30, 2018, was $505.8 million.

IHRTQ is currently in Chapter 11 bankruptcy reorganization.

iHeartMedia is acquiring Jelli for its programmatic radio advertising buying platform. Jelli already provides the technology for iHeartMedia's SoundPoint platform.

As iHeartMedia CEO Bob Pittman stated in the deal announcement,

Jelli allows us to do something no other company can do -- advertisers can now buy and use our broadcast assets, reach and impact just as they use the major digital players. We now offer heavy data and heavy creative innovation all in one place. We are excited about having Jelli not only for the platforms they are creating and have created for us, but also to lead our aggressive and innovative ad tech development.

In the past 12 months, IHRTQ's stock price has dropped *51.7%* vs. the S&P 500 Index' rise of *1.5%*, as the chart below indicates:

Source: [Seeking Alpha]()

With the deal for Jelli, IHRTQ management hopes to combine its reach and assets with Jelli's programmatic ad-buying capabilities to enable audio advertisers to reach much larger audiences through a single interface.

Although radio advertising is flat, podcasting usage is growing significantly, providing the combined companies with potential sources of growth, although still small in relation to iHeartMedia's radio station assets.

Ominously, the effect of Google adding audio streaming inventory to its offerings may be a serious competitor to the new combination.

Only one analyst is currently providing a rating on the stock, limiting IHRTQ's potential to get their message out to the broader investment community. The analyst currently has a 'Hold' rating on the stock.

In July 2018, a report surfaced that Liberty Media had an interest in purchasing a stake in IHRTQ, along with private equity firm Silver Lake.

Since then, public information about buyer interest has dropped off. Management continues to make smaller acquisitions while still under the cloud of bankruptcy administration.

Interested investors will likely need to wait until there is greater visibility into iHeartMedia's future.