Powering Progress with GovTech

Lincoln International's government technology (GovTech) market observations highlight the increasing preference of government agencies for integrated software solutions, driven by the need for efficiency, reliability, and coordination. There is significant growth potential in the GovTech market, fueled by cloud migration, federal support and strategic M&A activities, with valuations showing resilience and upward trends.

In this series, Lincoln International delves into the GovTech market, exploring its innovative solutions, trends, opportunities and positive impact on public sector operations.

LINCOLN
INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in

In the first volume of this series, our experts explore why government agencies prefer integrated solutions as well as value-creation opportunities for vendors, acquirers and private equity (PE) firms.

Government Agencies Prefer Integrated Solutions

Government decision-makers are pushing toward consolidating their technology needs across jurisdictions, departments and agencies, providing an excellent opportunity for a full-suite government software player to capture significant market share.

Government agencies rely on a myriad of systems to facilitate daily operations. Each of these systems can be sold as standalone point solutions, but many government agencies prefer to consume them from a single, consolidated vendor.

Below is a look at an illustrative government agency tech stack. These systems monitor the back-office details for revenue-generating segments and can integrate with payment processing solutions to enable real-time reconciliation and increased data accuracy.

LINCOLN
INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in

Benefits of an Integrated Platform

Government agencies' preference for one platform makes purchasing from an existing vendor favorable, faster, and much easier, driving a fertile cross-sell strategy.

Ease of Use: By providing one centralized portal for all back-office functionality, integrated platforms reduce the potential for user errors, simplify training and decrease the investment required for support / maintenance.

Efficiency: Agencies are often resource-constrained, especially when it comes to IT personnel / budgets. Using one vendor simplifies procurement, maintenance, training, integration, etc. and reduces the total cost of ownership.

Power of Integrated Apps: Real-time reconciliation across applications provides a better customer experience, reducing / eliminating highly manual / time-intensive reconciliation processes and increasing data accuracy across all functions.

Common Buying Center: The selection process for small government agencies is centralized around a single decision-maker, reducing the need for interdepartmental buy-in (e.g., budgetary, compliance, trust) when acquiring additional solutions.

Massive Value Creation Opportunity for GovTech Vendors, Strategic Acquirers and PE Firms

The potential for value creation driven by cross-selling, mergers and acquisitions (M&A) and organic growth is massive, proven and highly actionable as the industry is in the early innings of digitization and software adoption.

Cross-Selling Prospects: A natural cross-sell opportunity exists for any vendor that has multiple solutions, given customer preferences for an integrated platform.

Opportunity for Accretive M&A: Because cross-sell drives revenue synergies on top of cost synergies, more M&A targets are likely to be accretive.

Higher Retention Profiles: Customers who purchase multiple solutions from the same vendor tend to be stickier than those who purchase one solution.

Attractive Unit Economics: The cost of acquisition for smaller annual contract value customers can be more economically viable for Software-as-a-Service vendors because cross-selling of additional solutions can make them more profitable over time.

What is the Opportunity for Vendors, Strategic Acquirers and PE Firms?

The attractive buying behavior of government agencies makes this a market particularly ripe for value creation via cross-selling, accretive M&A and organic growth.

Factor Customer Preference into Valuation: For add-ons, feel more comfortable underwriting revenue synergies. For platforms, consider how add-ons can be more accretive than in commercial end markets.

Prioritize Growth Strategies Accordingly: Pursue add-on M&A more aggressively. Payments have proven to be a particularly successful cross-sell / growth opportunity.

Building vs. Buying: Consider creating instead of acquiring a product suite. As local government is less digitized, they have fewer product requirements. New product development efforts may not be so costly or long.

Avoid Common Pitfalls: Integrate products to reduce the burden on customers. Focus on the ideal customer profile / buying center as cross-selling is more successful when to the same buyer / type of customer.

> **"** Government decision-makers are pushing toward consolidating their technology needs across jurisdictions, departments and agencies, providing an excellent opportunity for a full-suite government software player to capture significant market share.

In the second volume of the GovTech series, Lincoln's experts explain how the sector represents a large, underserved market in the software industry with significant growth drivers fueling adoption and spending.

GovTech is a Large and Growing Market Ripe for Disruption

The public sector represents one of the most well-funded, yet underpenetrated, markets in software. This can be attributed to outdated systems, bureaucratic hurdles, long procurement cycles and resistance to change. The GovTech market is highly fragmented, with few providers of scale, and plenty of whitespace for innovators to capture significant market share. Further, multiple tailwinds continue to accelerate spend in new solutions, yielding a significant opportunity for vendors, acquirers and private equity (PE) firms.

Forecasted Global Government Software Market Size[1]

~10% CAGR

$77B

$40B

2023A

2030F

LINCOLN
INTERNATIONAL
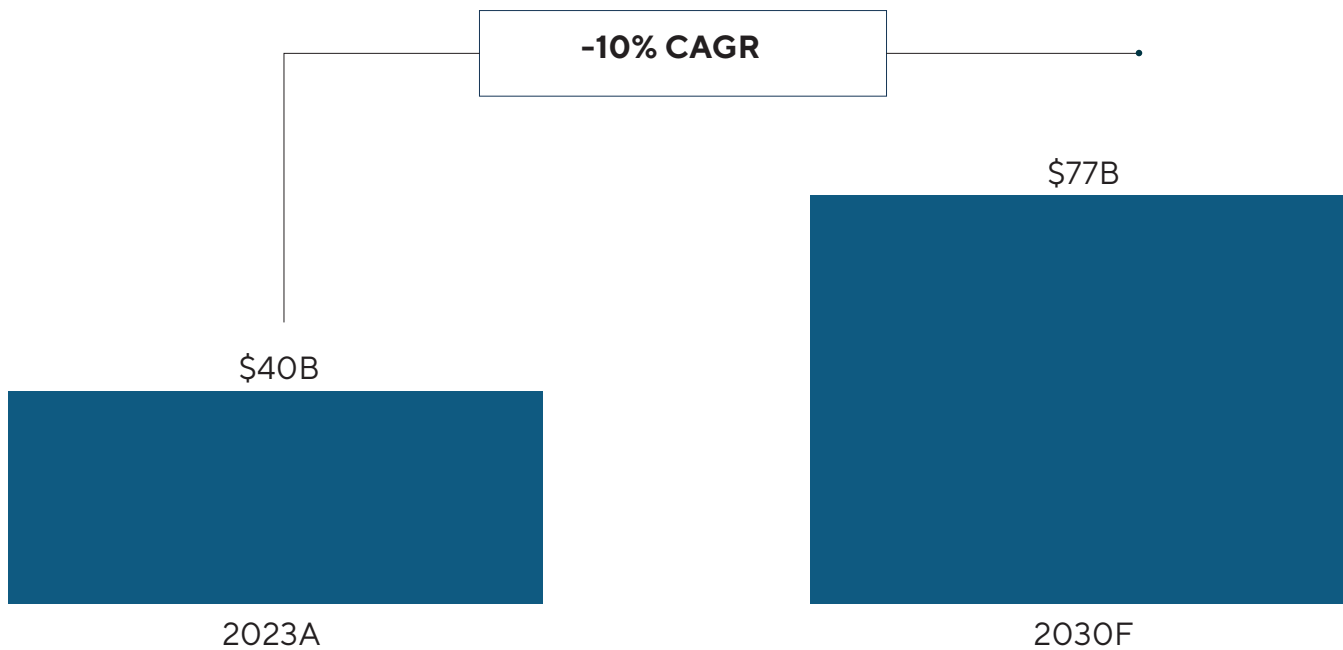
Government's Accelerating Investment in the Cloud[2]

GovTech is an expansive market early in the software adoption curve with multiple trends driving continued growth in the near term.

|	
~80%	Approximately 80% of on-prem ERP adopters are likely to migrate to a cloud-based solution in the next three to five years.
50%+	Over 50% of government IT leaders are developing cloud migration strategies for operational efficiency.
10%+	Cloud vendors for cities, counties and towns are experiencing 10%+ growth in Software-as-a-Service subscriptions.
$500B+	Federal support for cloud technology is at an all-time high, with $500 billion+ allocated for state and local digital infrastructure.
$1B+	Grants totaling $1 billion+ awarded to state and local governments to provide technical assistance & support to regional communities as part of the Build Back Better Regional Challenge, matched by $300 million in private funding.
50%	Some localities now have substantial "rainy day funds," reaching up to 50% of annual operating expenditures, indicating significant purchasing capacity.

Predictions for the GovTech Market[3]

75%

By 2025, 75% of governments will expand the adoption of cloud solutions to 50%+ of total spend.

78%
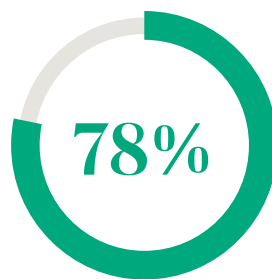
By 2026, 78%+ of government CIOs will increase investments to produce positive citizen experiences as a critical business outcome.

60%
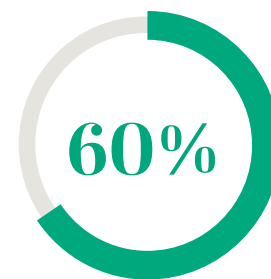
By 2026, 60%+ of government organizations will prioritize investing in business process automation, up from 35% in 2022.

GovTech Has Compelling Tailwinds Increasing Adoption and Spend

Strong market forces and strategic initiatives are propelling GovTech cloud adoption and investment.

Intensifying Demand for Purpose-Built Solutions

Under-digitization in local governments drives the need for modern cloud-native solutions.
50% of local governments still rely on outdated or homegrown systems, representing a ~$20 billion market segment that requires modernization to enhance efficiency and provide purpose-built functionality

Federal stimulus money (e.g., ARPA) supports stable budgets for local governments.
Massive amounts of funding are contributing to local government's continued digitalization movement.

Desire for increased transparency and efficiency resulting in the adoption of purpose-built software.
Public sector employees are demanding better efficiency and transparency, while citizens are seeking increased visibility into government operations, spending and revenue.

Labor shortages fueled by an aging workforce are incentivizing governments to leverage software to increase efficiency and productivity.
Government agencies are constantly looking for new ways of doing more with less amidst challenging labor markets.

COVID-19 and cyber threats drive governments toward secure, cloud-based solutions.
The shift to work-from-home due to COVID-19 and the increased threat of cyber-attacks are compelling governments to adopt fast, secure and effective cloud-based solutions.

Demand by citizens for modern, accessible and resilient solutions is accelerating.
Consumer expectations for easy-to-use, digital-first solutions have extended to all facets of daily life, including paying bills and accessing public resources.

Sources:

(1) Verified Market Reports; includes spend related to the creation, application, and upkeep of software solutions specifically designed to satisfy the particular requirements and needs of governmental bodies at all levels, including local, state and federal governments
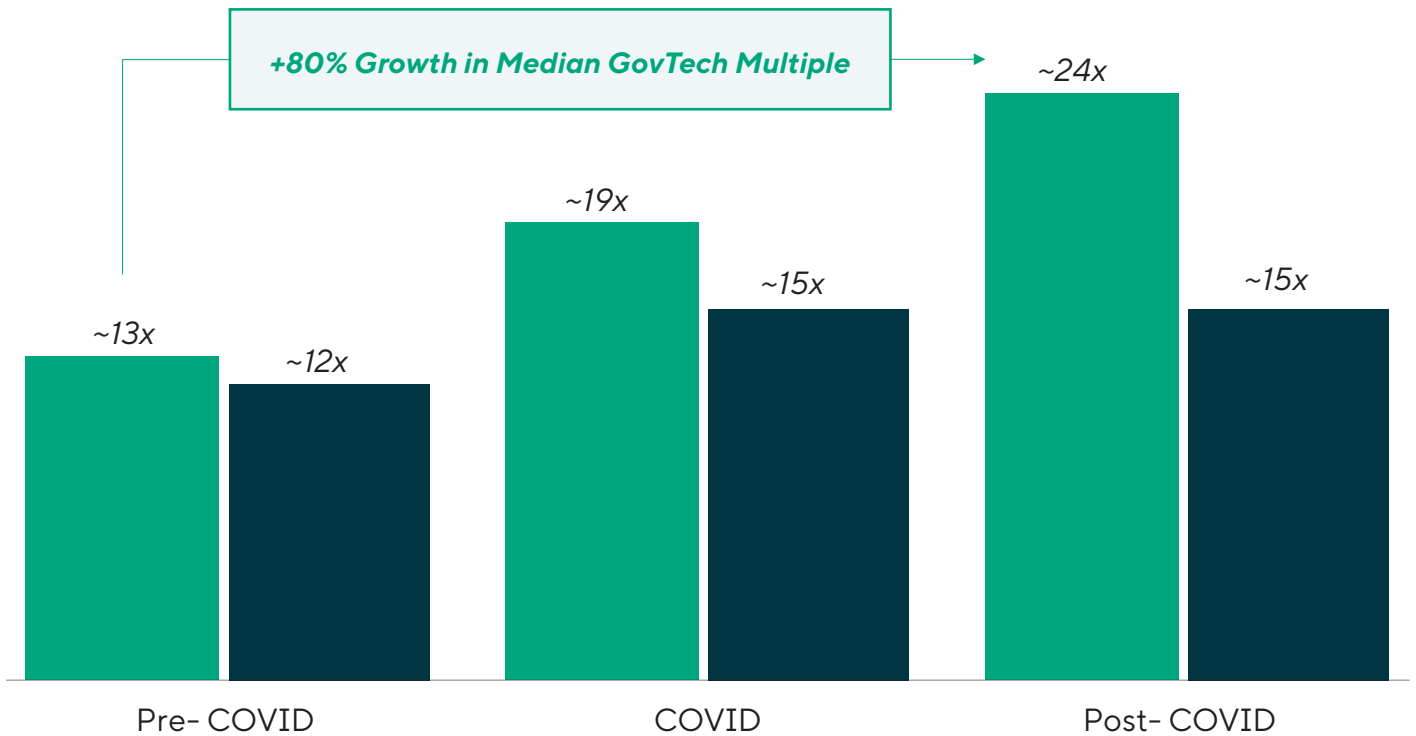
(2) Gartner

(3) Deloitte; Technology Business Research; NYS Office of the Controller; WhiteHouse.gov; Eda.gov

Volume Three: Booming GovTech Valuations

In volume three of our series, we explore how rising private equity interest has driven GovTech valuations and M&A activity to new heights.

Expanding GovTech Multiples

Recent transactions have showcased that acquirers have an appetite for the GovTech category and are willing to pay a premium for these assets, accelerating M&A activity and fueling valuations.

Precedent Transaction Median EV / EBITDA Multiples[1]

+80% Growth in Median GovTech Multiple

Pre- COVID: ~13x / ~12x
COVID: ~19x / ~15x
Post- COVID: ~24x / ~15x

~5x	~13x	~10x
GovTech deals per year	GovTech deals per year	GovTech deals per year

■ GovTech Transactions   ■ All SaaS Transactions

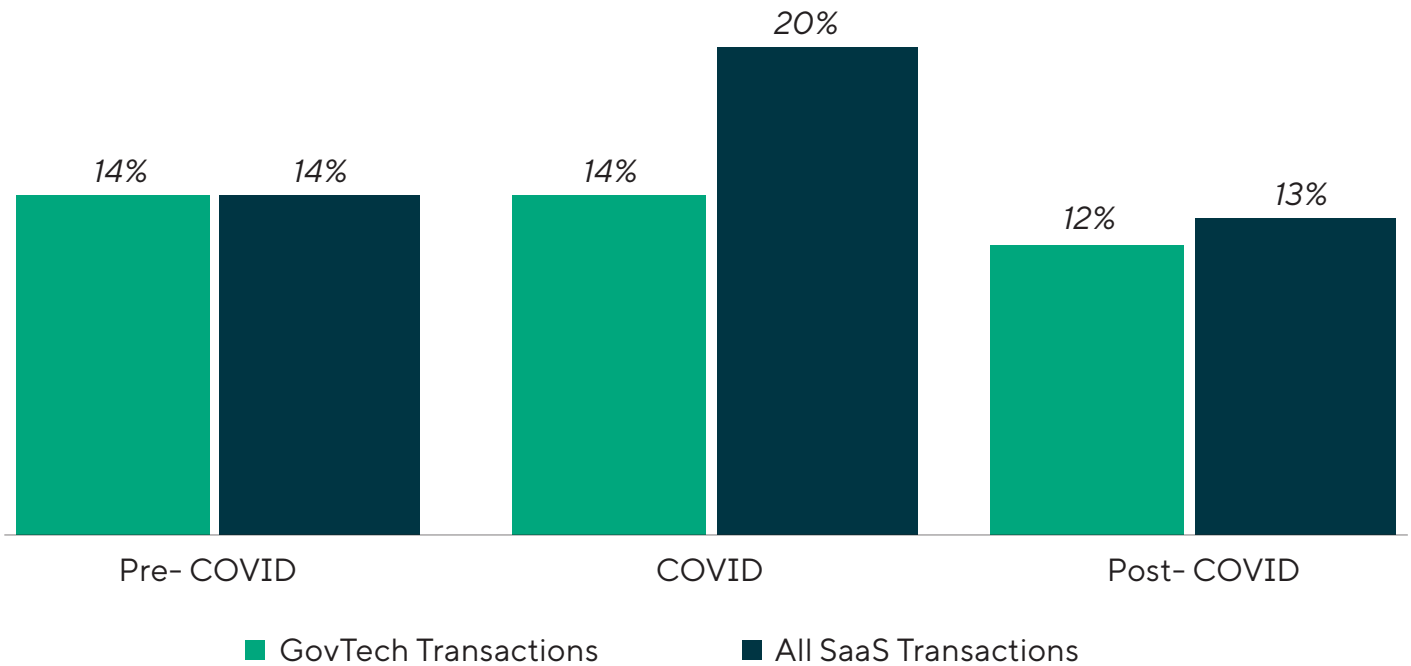**LINCOLN** INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com

GovTech's performance is consistent across periods and with that of broader SaaS vendors, implying recent premium is driven by market demand rather than a superior financial profile.

Precedent Transaction Median LTM Revenue Growth[1]

Pre- COVID: GovTech Transactions 14%, All SaaS Transactions 14%
COVID: GovTech Transactions 14%, All SaaS Transactions 20%
Post- COVID: GovTech Transactions 12%, All SaaS Transactions 13%

■ GovTech Transactions   ■ All SaaS Transactions

Precedent Transaction Median EBITDA Margin[1]

Pre- COVID: GovTech Transactions 31%, All SaaS Transactions 29%
COVID: GovTech Transactions 31%, All SaaS Transactions 25%
Post- COVID: GovTech Transactions 29%, All SaaS Transactions 28%

■ GovTech Transactions   ■ All SaaS Transactions

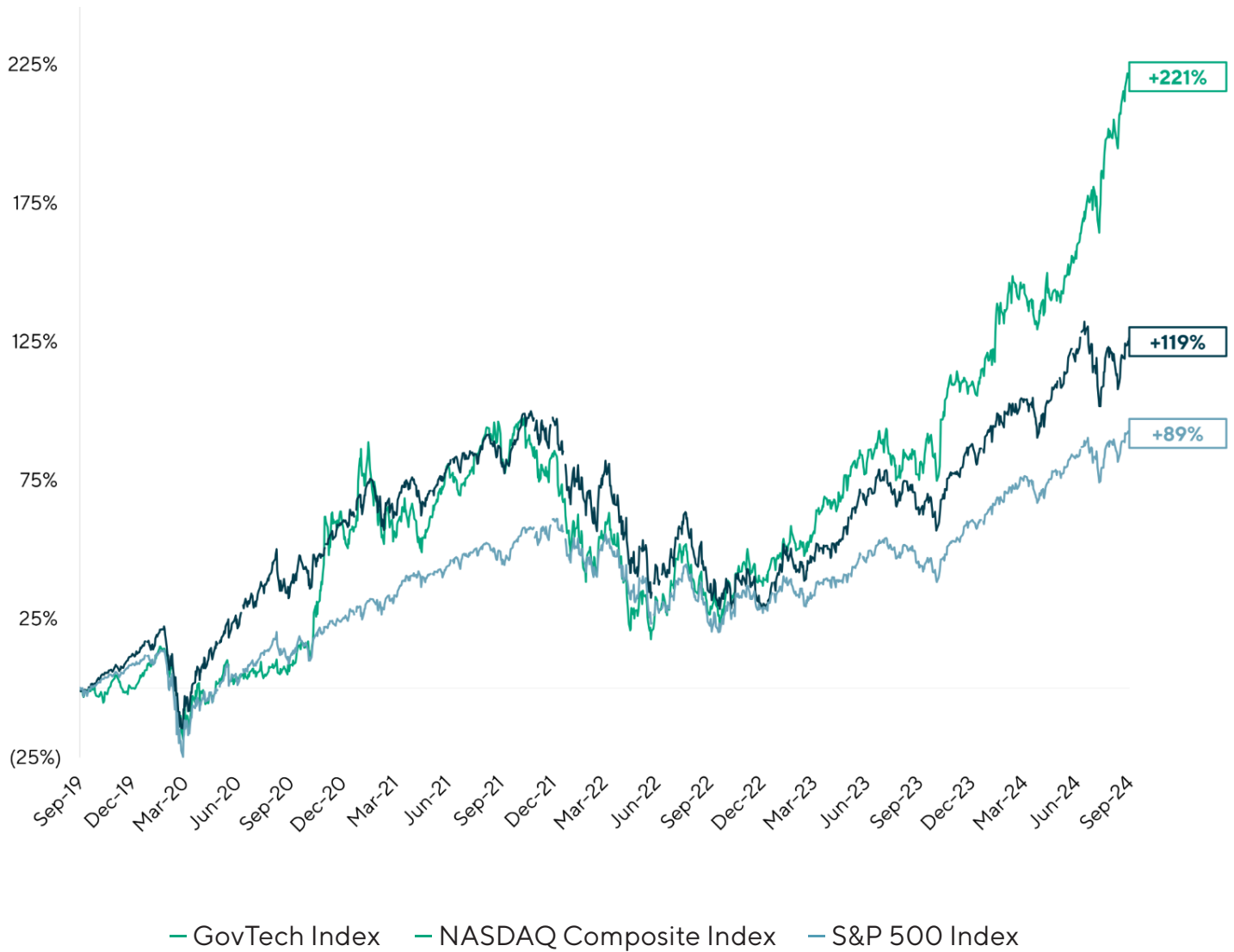LINCOLN INTERNATIONAL
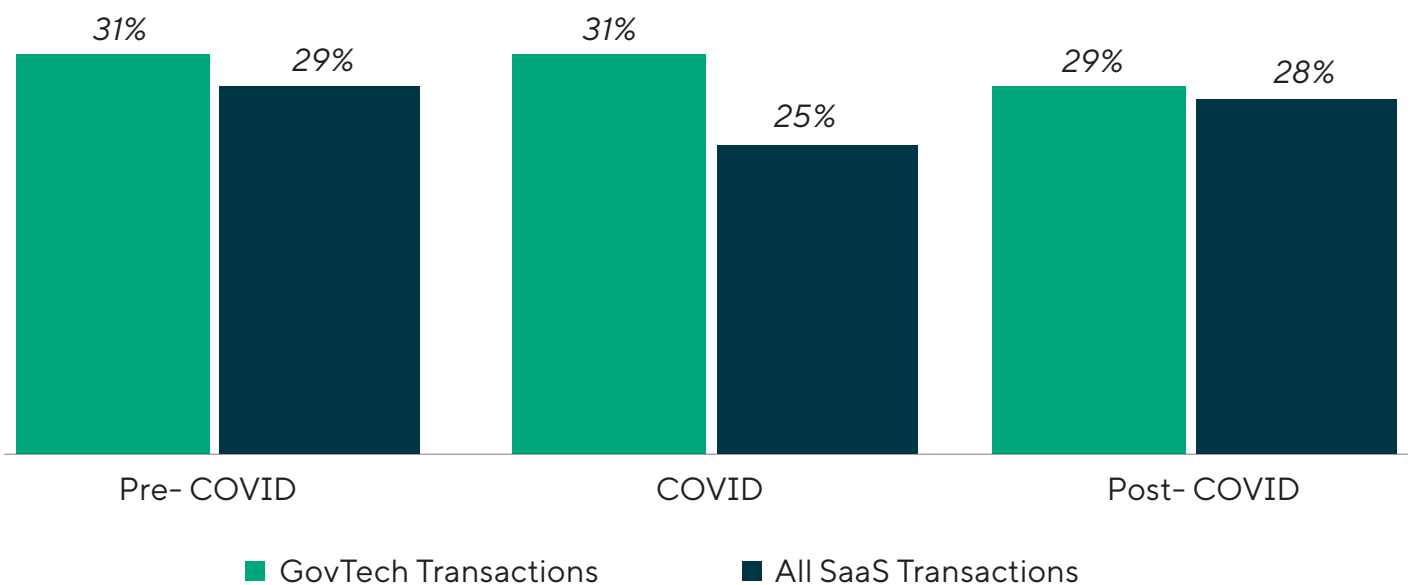
Public Markets Mirror Private Market Demand for GovTech Across Economic Cycles
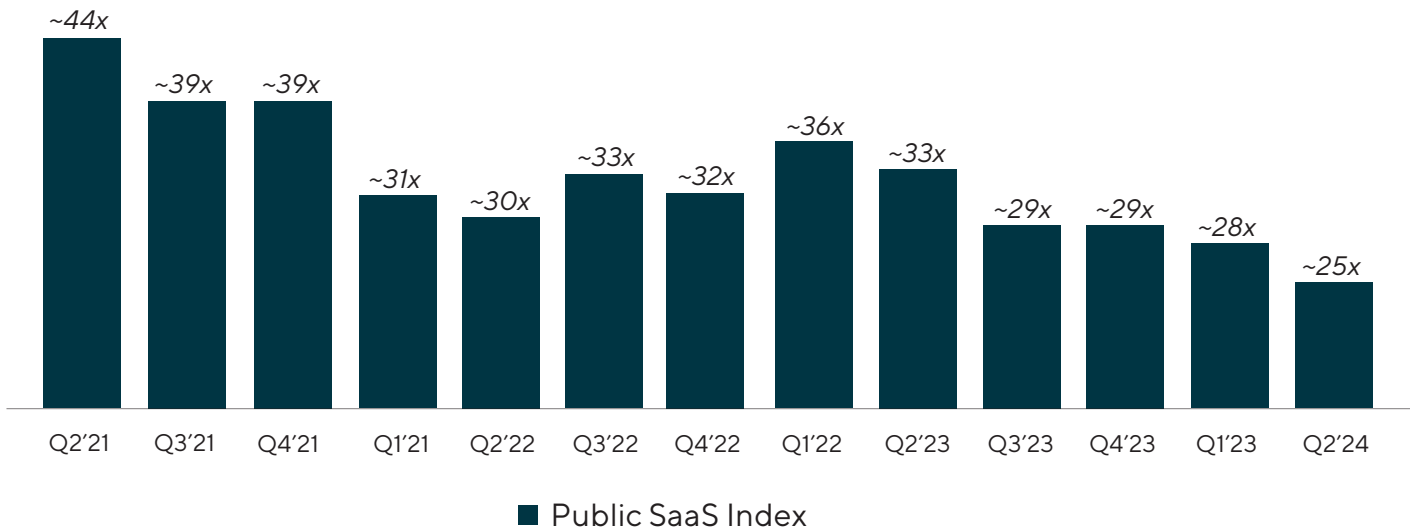
GovTech has outperformed both the S&P 500 and the more traditionally tech-heavy NASDAQ over the past five years, showing resiliency over the last 24 months as other market valuations have contracted. Public markets resemble the private markets in showcasing the value investors place on GovTech assets.

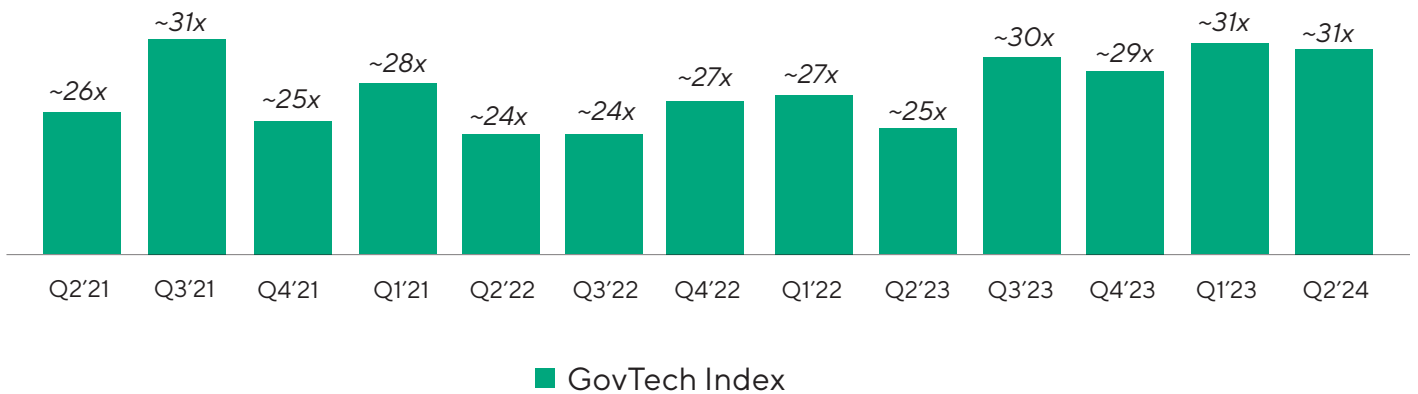## Public GovTech Index – 5-Year Trading Performance[1][3]

— GovTech Index   — NASDAQ Composite Index   — S&P 500 Index

LINCOLN
INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in

Public GovTech Index – 3-Year EV / NTM EBITDA Trending[1][3]

(43%) contraction in public SaaS EBITIDA multiples

Q2'21	Q3'21	Q4'21	Q1'21	Q2'22	Q3'22	Q4'22	Q1'22	Q2'23	Q3'23	Q4'23	Q1'23	Q2'24
~44x	~39x	~39x	~31x	~30x	~33x	~32x	~36x	~33x	~29x	~29x	~28x	~25x

■ Public SaaS Index

+20% growth inthe GovtTech Index EBITDA multiples

Q2'21	Q3'21	Q4'21	Q1'21	Q2'22	Q3'22	Q4'22	Q1'22	Q2'23	Q3'23	Q4'23	Q1'23	Q2'24
~26x	~31x	~25x	~28x	~24x	~24x	~27x	~27x	~25x	~30x	~29x	~31x	~31x

■ GovTech Index

Why are GovTech Valuations Attractive?

Investors find GovTech valuations desirable for the following reasons:

	Dependability of the Customer Base	• **Premier retention profile** provides **downside protection** for buyers **and lenders** • **Stable budgets dynamics** result in **consistent spend throughout business cycles**
	Sustainability & Predictability of Growth	• **The digital wave is here**, but slow sales cycles have deferred adoption leaving **untapped potential yet to be realized** • Public sector's growing preference for integrated solutions enables vendors **to underwrite revenue synergies via cross-sell**, providing a reliable growth vector in a **highly fragmented market**
	Significant Market Tailwinds	• **Huge addressable market** that is **underdigitized** – significant opportunity remains for **greater IT spend and adoption** • **Digitization trend** is driven by **IT paradigm shifts** such as **cloud adoption** and a **greater need for cybersecurity** • **Expectations for improved technology** are driven by a more **digital-native citizenry and government workforce** • Demand is addressed by tremendous amounts of **federal and state funding earmarked for government IT spend**

LINCOLN INTERNATIONAL

	Attractive Customer Preferences	• Governments continue to **favor reliable, "good enough"** solutions, **reducing the need for R&D investment** and **lowering the risk of disruption** from newer, more innovative products • **Strong network effect** facilitates **viral new logo growth** • Small-to-medium sized local governments prefer a consolidated platform, yielding **massive cross-sell opportunity**
	Operating Leverage Throughout the P&L	• **COGS:** sticky customer base with **high switching costs and low incentives to change** • **R&D:** minimal demand for product improvements in **well-established product categories** enables vendors to maintain lower R&D budgets • **S&M:** prospective customers / decision-makers are **identifiable / accessible**, and share best practices to enable **viral customer adoption**

LINCOLN
INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in

In the fourth volume of this series, Lincoln explains why U.S. government agencies are attractive customers, making GovTech vendors particularly valuable to financial and strategic buyers alike.

Government Customers Have Highly Attractive Characteristics

The 90K+ government agencies in the U.S.(1) represent a highly attractive customer profile due to their long lifetimes, centralized decision-making, and collaboration on best IT practices.

Word of Mouth Heavily Influences Local Governments
How / Why Government Customers Drive Viral Adoption

Alignment	**Standardization**	**Risk Management**
Unlike the commercial sector, government entities do not compete, so they share best practices.	The need for coordination between neighboring / overlapping encourages agencies to use common IT systems.	Governments tend to be more risk-averse than commercial customers, so they prefer vendors that are proven with peers.

Implications for GovTech Vendors

	Local GovTech is a Direct Sales Market	May require physical presence in key geographies to gain traction among clusters of prospects / customers.
	Leverage GovTech Communities	GovTech conferences are plentiful and valuable for building a brand in local government networks.
	Customer Success is Key	Critical to deliver on implementation / support to provide a positive experience that will enable viral adoption.
	Capitalize on Collaboration	Emphasize customer testimonials / references / referrals wherever possible.
	Consider M&A to Enter New Markets	Can be much more efficient / actionable to enter a new market via acquisition of an existing vendor than to seek to establish a footprint from scratch.
	Start Small	May be necessary to build a presence in a region via smaller customers to start before leveraging them to access larger customers.

GovTech vendors benefit from viral customer acquisition, resulting in a highly efficient GTM.

LINCOLN
INTERNATIONAL

Government Agencies Are Highly Retentive
Gross Dollar Retention from Lincoln's Recent GovTech Transactions

	96%	97%	95%	98%	99%	93%	98%	99%
	Deal 1	Deal 2	Deal 3	Deal 4	Deal 5	Deal 6	Deal 7	Deal 8
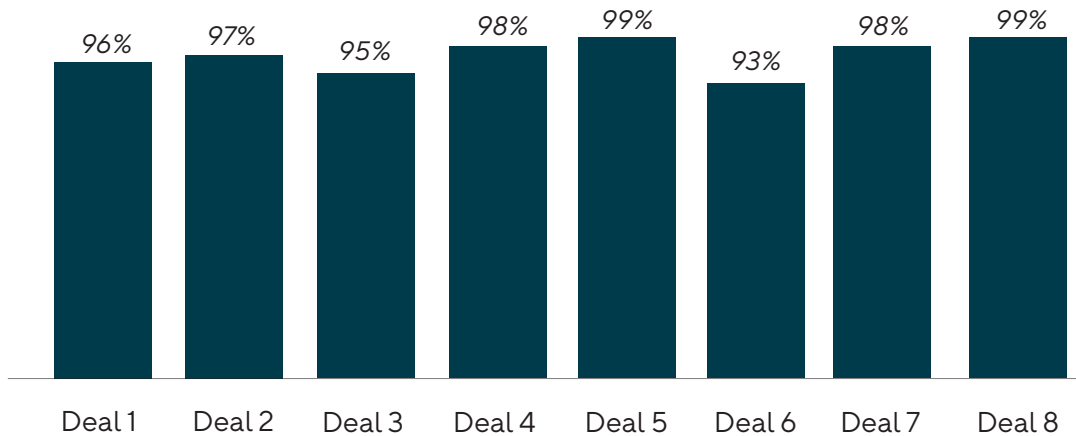
Intensifying Demand for Purpose-Built Solutions

Slow / Bureaucratic Decision Making: Processes for approving new software can be lengthy and complex.

Long-Term Contracts: Most federal agencies opt for long-term vendor agreements.

User Training / Familiarity: Government employees are relatively averse to change, feeding preference for existing systems

High Switching Costs: Changing systems involves significant time, effort, and financial resources.

GovTech vendors benefit from high customer stickiness, yielding highly profitable customer lifetime values due to long tenures and diminished support / R&D obligations

Source:

(1) 90K+ government agencies consists of federal agencies, state governments, municipalities, counties, school districts and other special purpose local governments. Figures sourced from USA.gov, US Census and the St. Louis Federal Reserve

LINCOLN INTERNATIONAL

Government Agencies Present a Highly Attractive Cross-Sell Opportunity

Government decision-makers are increasingly pushing toward standardizing on one vendor platform across jurisdictions, departments, agencies, etc. providing the opportunity for a full-suite software vendor to capture significant market share.

Cross-Sell Yields Highly Attractive Unit Economics...
Illustrative Customer Journey for a Government Agency

1	2	3	4	5
Initial Purchase	Organic Expansion	Cross-Sell of Complementary Solutions	Monetizing Payments	Fully Penetrated Spend
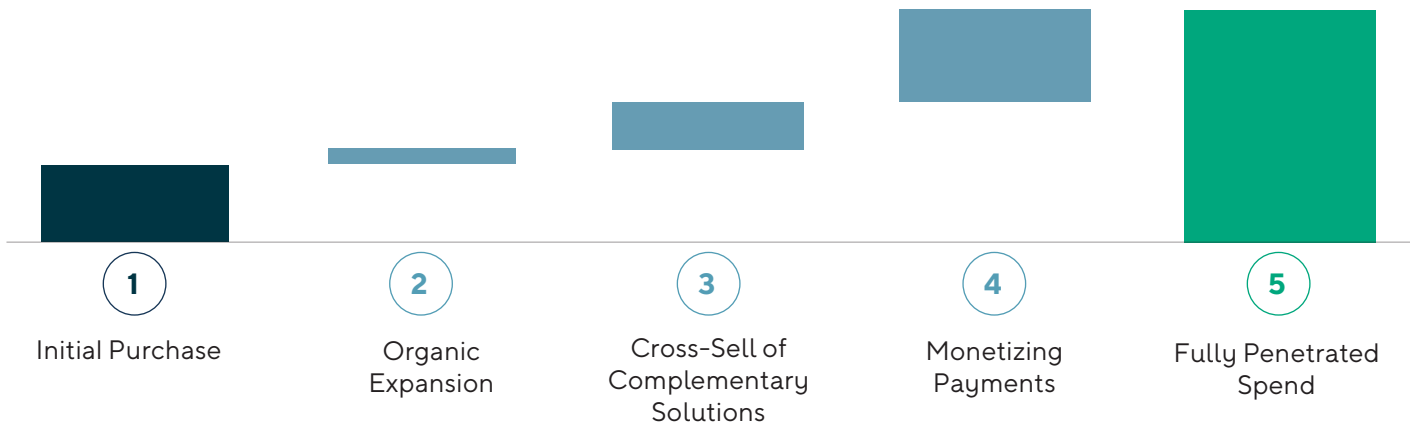
1 | Agency identifies core need and chooses vendor through word-of-mouth research and careful vetting process.

2 | Over time, agency naturally finds need to expand number of seats and adopt cloud technology.

3 | Agency discovers additional needs; contemplates existing vendors due to built-in trust, implementation speed, and likelihood of budgetary approval.

4 | Agency consolidates workflow software and payments to fully integrate technology stack and improve transparency of revenue reporting.

5 | Fully penetrated spend, capturing all whitespace and maximizing customer-level profitability.

> GovTech customers who start small at sign-on can be highly economically valuable / profitable over time.

...and Efficient Go-to-Market Strategies
S&M Efficiency Statistics from Recent Lincoln GovTech Transactions
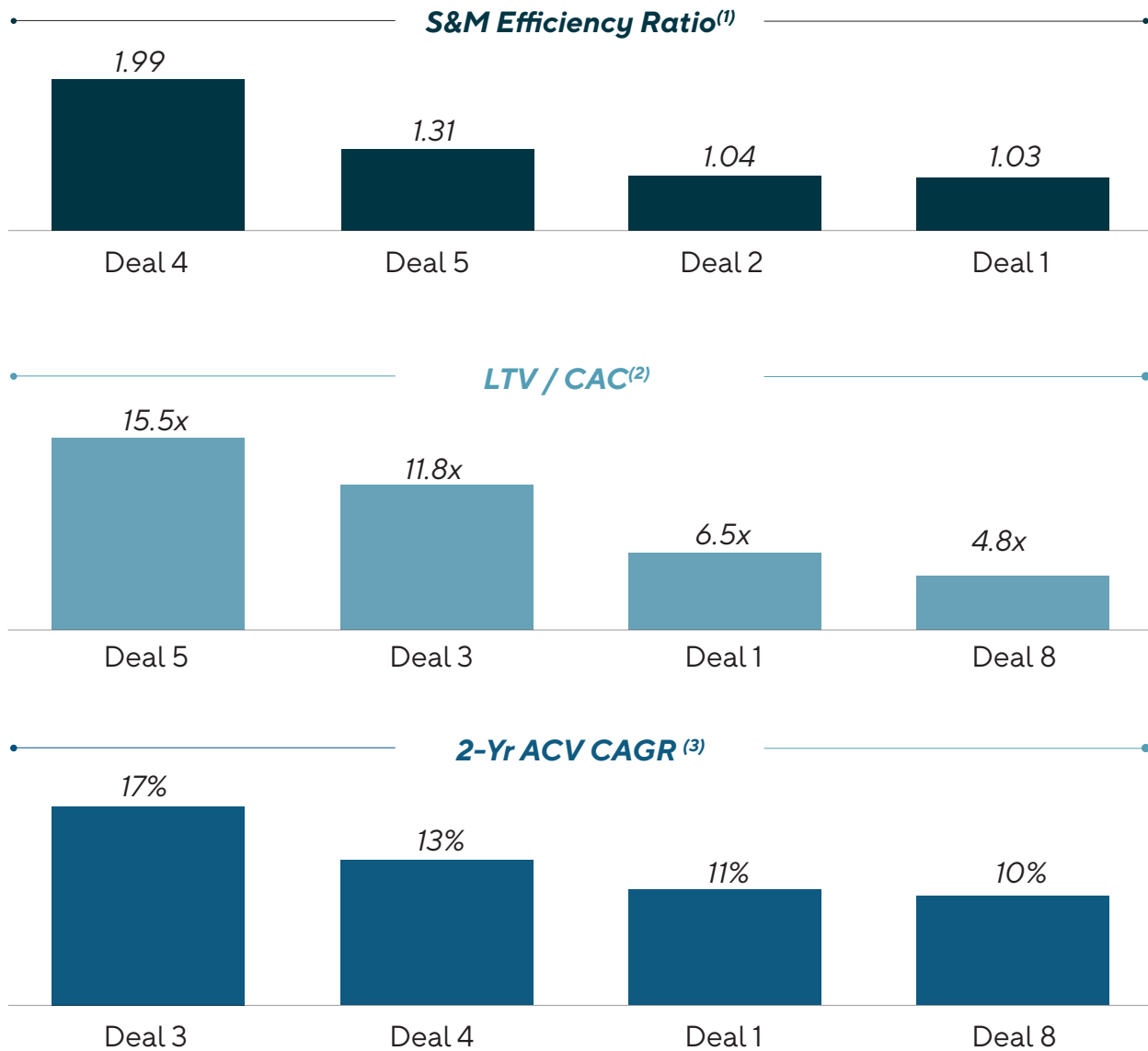
S&M Efficiency Ratio[1]

Deal 4	Deal 5	Deal 2	Deal 1
1.99	1.31	1.04	1.03

LTV / CAC[2]

Deal 5	Deal 3	Deal 1	Deal 8
15.5x	11.8x	6.5x	4.8x

2-Yr ACV CAGR[3]

Deal 3	Deal 4	Deal 1	Deal 8
17%	13%	11%	10%

Government agencies preference for one platform makes purchasing from an existing vendor favorable, faster and much easier, driving a fertile cross-sell strategy and highly attractive unit economics.

Sources:

(1) LTM Recurring Revenue Bookings / LTM S&M Expense
(2) Lifetime Value / Customer Acquisition Cost
(3) Average Recurring Revenue Contract Value for 1 Year

LINCOLN INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in

Multiple Areas to Realize Operating Leverage Throughout the P&L

The unique characteristics of the GovTech market underpin opportunities to create value across a GovTech vendor's entire organization. Reference the key below to align with income statements.

	Summary Income Statement	% of Revenue
1	**New Bookings**	**N/A**
2	**Existing Bookings**	**N/A**
3	*Gross Dollar Retention*	*95%+*
	Net Dollar Retention	*108%+*
	ARR	**N/A**
	ARR Growth %	*10–20%*
4	Recurring Revenue	85%+
	Non-Recurring Revenue	< 15%
	Total Revenue	**N/A**
5	Cost of Goods Sold	< 25%
	Gross Margin %	**75%+**
6	(–) S&M Expense	10–20%
7	(–) R&D Expense	10–20%
	(–) G&A Expense	~10%
	Total Operating Expenses	**30–50%**
8	**Adj. EBITDA Margin %**	**25–50%**

1	**Stable New Bookings**	While sales cycles are long, **lower ACVs** associated with small local governments **yield bookings stability**
2	**Attractive Existing Customer Monetization**	Stellar net retention due to **customer propensity to buy multiple products, ability to extract price increases, payments adoption, cloud migration**, etc.
3	**Sticky Customer Base**	Slow and bureaucratic decision-making fosters **high retention rates**, as there is **little incentive to switch** technology providers once chosen
4	**Predictable Revenue Streams**	High retention and recurring revenue percentages **drive strong revenue visibility**
5	**Low Cost to Support**	Customer stickiness **reduces support obligation**
6	**Efficient GTM**	Leverage **shared incentives** and collaboration across non-competing public sector clients to drive **viral customer acquisition** and **seamless "land and expand" growth**
7	**Minimal Demand for R&D Innovation**	GovTech customers **prioritize "good enough"** solutions over "cutting edge" technology, with **modest expectations** and **no need to evangelize** established product categories
8	**Robust EBITDA Margins**	The combination of **top-line predictability** and **operating efficiency** enables GovTech vendors to enjoy **healthy and consistently expanding margins**

GovTech vendor operating leverage has powered outstanding returns for the private equity community over the past decade+ and continues to attract tremendous interest.

LINCOLN INTERNATIONAL

In the sixth volume of the GovTech series, Lincoln's experts explore the transformative impact of cloud technology on government operations. This volume highlights the key tailwinds and growth drivers pushing government cloud adoption and investment.

Compelling Tailwinds Increasing Government Cloud Adoption and Spending

Growing government investment in cloud technology is being driven by a combination of internal and external forces.

Intensifying Demand for Purpose-Built Solutuions

External Macro-Level Tailwinds				Internal Initiatives Spurring Adoption
Labor shortages are incentivizing governments to leverage software and outsource IT management to **increase efficiency and productivity**	**Increased threat of cyber attacks** are pushing governments to evaluate **secure, cloud-based solutions** which offer **regular updates** and **advanced threat detection / prevention**	The **rise of remote work,** accelerated by the COVID-19 pandemic, **exposed vulnerabilities** in legacy systems and drove demand for **flexible, cloud-based collaboration tools**	Some large GovTech vendors (e.g., Harris, Tyler, etc.) are **sunsetting legacy solutions**, pushing governments to **evaluate alternatives**	**Desire for increased transparency and efficiency** resulting in **adoption** of purpose-built software
Federal stimulus money (e.g., ARPA) supports **stable budgets** for local governments	Adoption of cloud systems has become a **catalyst for governments to switch vendors,** overcoming inertia that might have kept them on legacy products, and driving **new logo growth for vendors**	Broader market shift by most vendors to cloud-based subscription agreements given the **significant uplift in ARR these models provide**, ensuring **more predictable,** recurring revenue streams	**Centralized data storage, real-time** processing and **scalable computing power** enables **enhanced data analytics** at a lower cost and greater ease of use than on-premise solutions	Desire **for remote access and limited downtime from on-prem outages** driving governments to adopt **cloud-native solutions**

Government's Accelerating Investment in the Cloud

Federal and local government grants, subscriptions and investments in cloud technology are growing rapidly. Initiatives aimed at operational efficiency and an increased purchasing capacity are propelling this accelerating growth.

50%+	Over 50% of government IT leaders are **developing cloud migration strategies for operational efficiency**
10%+	Cloud vendors for cities, counties and towns are experiencing **10%+ growth in SaaS subscriptions**
$500B+	Federal support for cloud technology is at an all-time high, with $500B+ allocated for state and local digital infrastructure
$1B+	**Grants of $1B+** awarded to state and local governments as part of the Build Back Better Regional Challenge, matched by **$300M in private funding**
50%	Some localities now have substantial "rainy day funds," reaching up to **50% of annual operating expenditures, indicating significant purchasing capacity**

Sources: Deloitte; Technology Business Research; NYS Office of the Controller; WhiteHouse.gov; Eda.gov

Cloud is Coming

Government agencies are increasingly adopting cloud solutions, with leaders driving adoption in areas like citizen engagement and HR. As legacy challenges and compliance hurdles ease, SaaS adoption is set to accelerate dramatically over the next decade.

Business Value (vertical axis)

Level of Cloud Adoption (horizontal axis)

Ad-Hoc / Explorational
- Minimal SaaS adoption, often limited to basic tools like email or single-use applications.
- Fear of disruption or lack of technical expertise hinders progress

Define/ Repeatable
- Hesitant to move beyond pilots and POC SaaS projects
- Concerns over data sovereignty and privacy slow adoption
- May still rely heavily on legacy systems but are starting to shift to hybrid cloud models

Managed/ Aligned
- Mix of cloud and legacy systems
- Adoption is driven by a desire for cost efficiency, scalability and modernization
- Focus remains on compliance and risk mitigation

Adoption/ Migration
- Adopt proven SaaS solutions guided by formal cloud policies (e.g., cloud-first)
- Use SaaS to modernize legacy systems and improve operational efficiency

Optimization/ Modernization
- Leverage cutting-edge technologies to optimize operations and capabilities

Government agencies are at an inflection point on the cloud adoption curve, having realized the operational benefits of adopting cloud-based solutions, but have yet to migrate to being fully cloud native

GovTech is at an inflection point on the cloud adoption curve, driven by cloud-first mandates, advanced SaaS solutions and rising citizen demands for digital services

Ready to discuss the opportunities ahead for you?
Connect with a senior professional at connect@lincolninternational.com

LINCOLN INTERNATIONAL

REAL CONNECTION. TRUE PERSPECTIVE.
Connect with us at www.lincolninternational.com | in