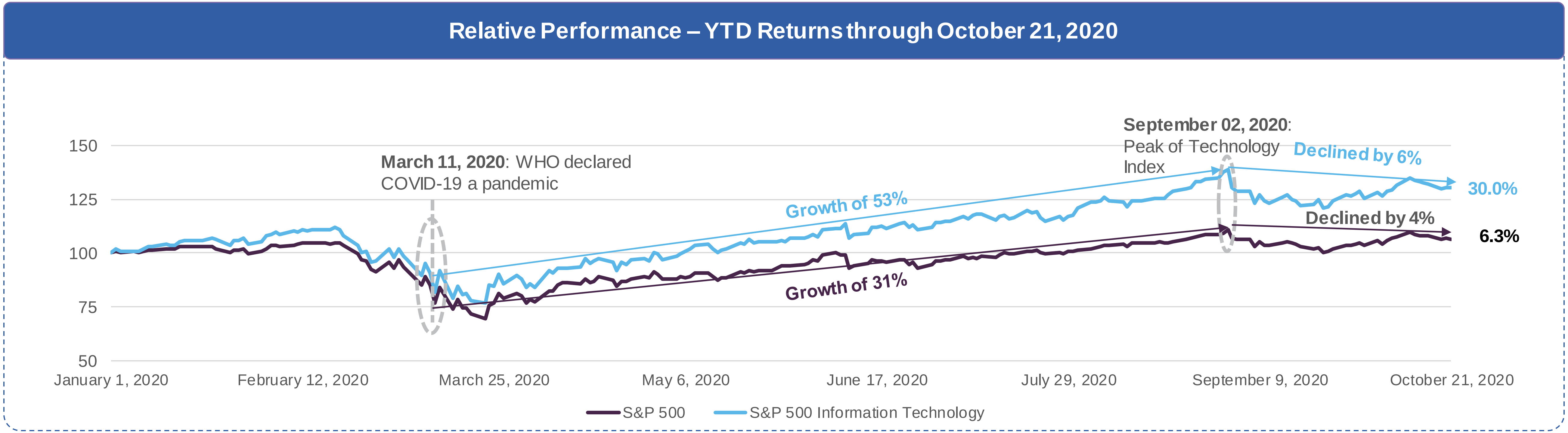
Technology Sector Q3 2020 Update

Corporate and Investment Banking Practice

Technology sector has significantly outperformed most other sectors

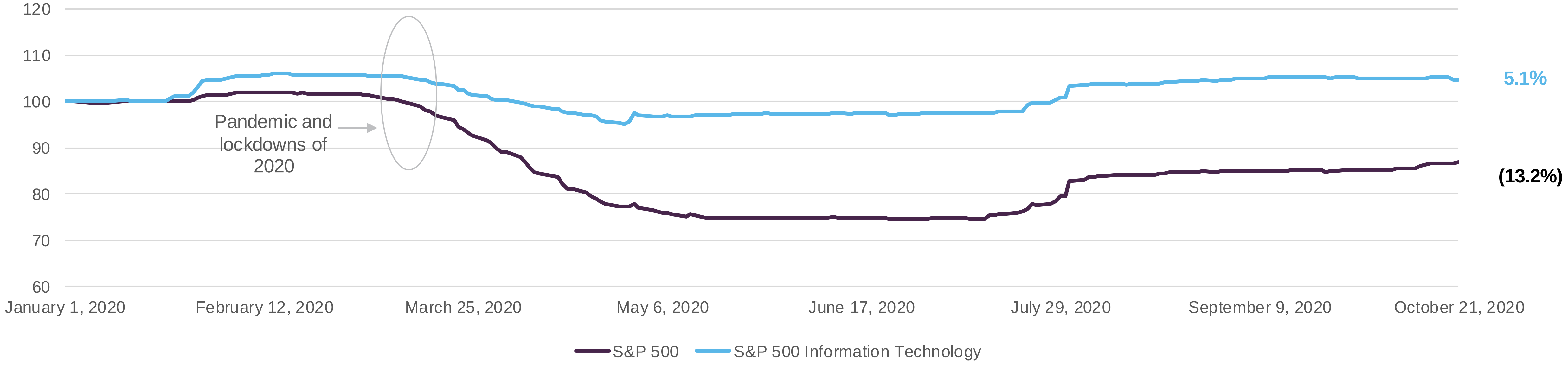


Source: S&P Dow Jones Indices website

- Technology stocks have witnessed unprecedented gains in recent months
  - As of October 21, 2020, the S&P 500 Information Technology index reported a remarkable 30% increase since the beginning of 2020
  - Both software and hardware stocks significantly outperformed those of most other industries during the COVID-19 pandemic
- However, there is a widespread concern of a tech bubble and continued worries around tech stock valuations being too high
  - In contrast to the dot-com bubble (in the late 1990s when tech-valuations were very high), the current growth in the technology sector has been supported by strong earnings delivery and is reflective of the increased demand for "essential" services, strong balance sheets, superior profitability, and consistent free cash flow generation
- As of October 21, 2020, the tech index witnessed about 6% correction, after it had peaked on September 2, 2020 levels
  - This was mainly due to uncertainty around the new US fiscal stimulus, as well as rising number of global coronavirus cases (due to second and third wave of COVID-19)

Fundamentals are supportive; earnings estimates for technology sector have moved above their pre-pandemic highs

NTM EPS Forecast

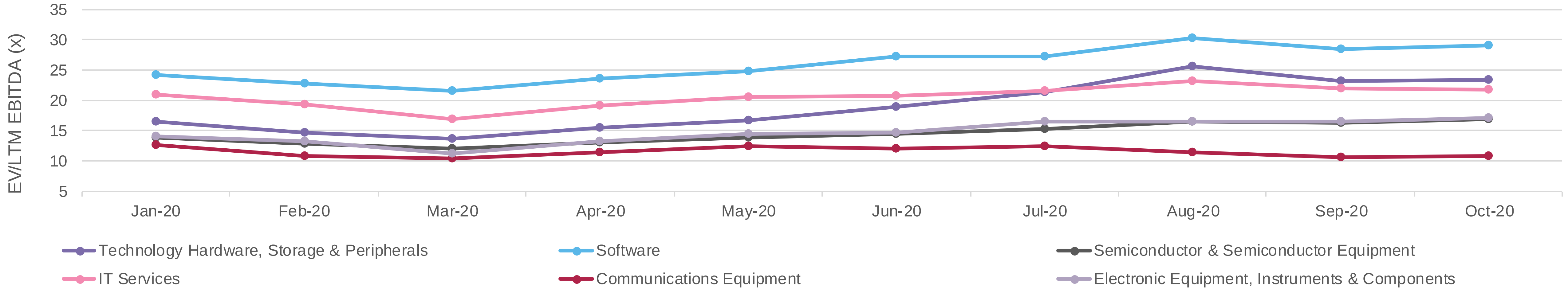


- Consensus estimates expect 5% earnings growth for the technology sector in 2020, the best among the earnings growth of all 11 S&P 500 sectors
  - Earnings for S&P 500 technology companies is likely to decline by just 0.6% from that in the previous year's third quarter, the smallest decline among all sectors. Earnings for the entire S&P 500 is expected to fall by 21.3% y-o-y in Q3 2020
  - In fact, apart from healthcare and utilities, technology was the only other sector to produce earnings growth in in Q2 2020
- These earnings justify the sector's premium valuation
  - The tech sector is trading at a PE ratio of ~24.0x estimated 2021 earnings, which is ~22% above that of the broader S&P 500 g roup
  - The sector accounts for 15% of trailing 12-month S&P 500 earnings and an even higher proportion of forecast earnings (20% of 2023 earnings)

Source: S&P Dow Jones Indices w ebsite

Technology sub-sector valuations witnessed upward trend during Q3 2020

Technology Sub-sectors Valuations – EV/LTM EBITDA through October 21, 2020



Software

- ✓ Software has outperformed other tech verticals
  - Rapid digital transformation and migration to cloud has enabled significant growth for cloud companies, such as Salesforce.com and ServiceNow

Semiconductor & Semiconductor Equipment

- ✓ Sustained momentum through Q3 2020
  - Logic and memory sub-segments showed resilience, owing to continued investment in data centers and hardware sales to support work-from-home, gaming, and 5G phones
  - Weak auto and industrial markets affected the analog and microcontroller verticals

Hardware, Storage & Peripherals

- ✓ Hardware segment has benefited from work-from-home trends
  - Increase in demand for PCs for home entertainment and distance learning, as a result of the COVID-19 pandemic
  - Cloud-related IT infrastructure investments will help the segment to remain resilient over the years

IT Services

- ✓ IT services expected to remain slow
  - Digital transformation continues across businesses, with IT spending focused on projects to ensure employee productivity
  - Growth-oriented projects that have longer payback periods have largely been delayed

Source: S&P Dow Jones Indices w ebsite

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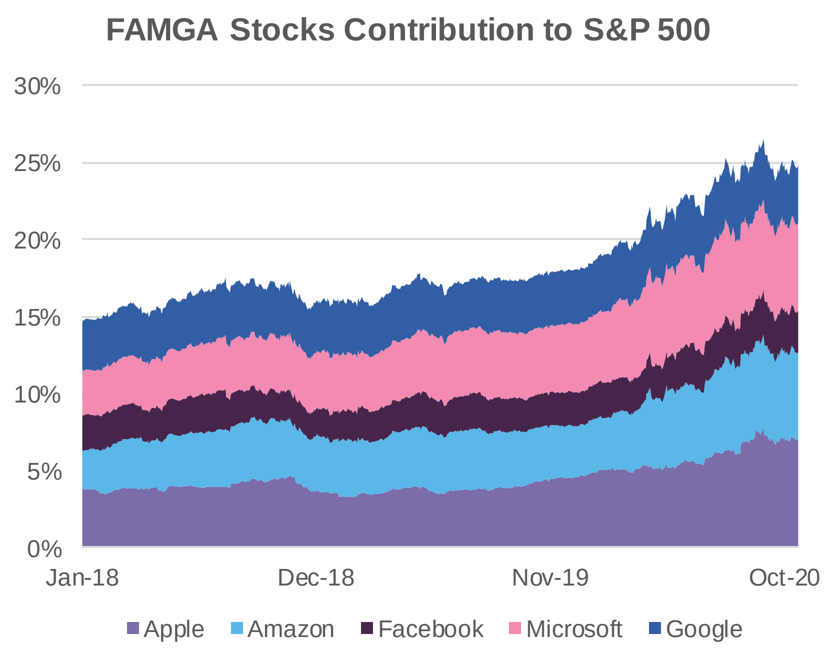
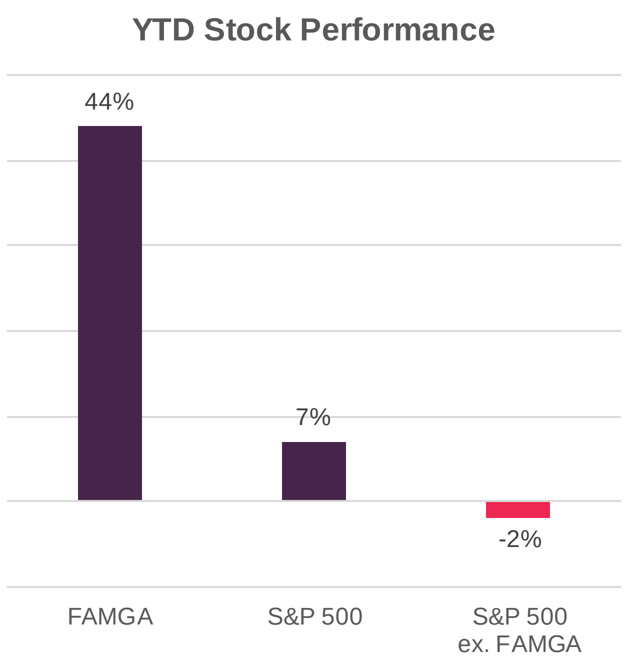
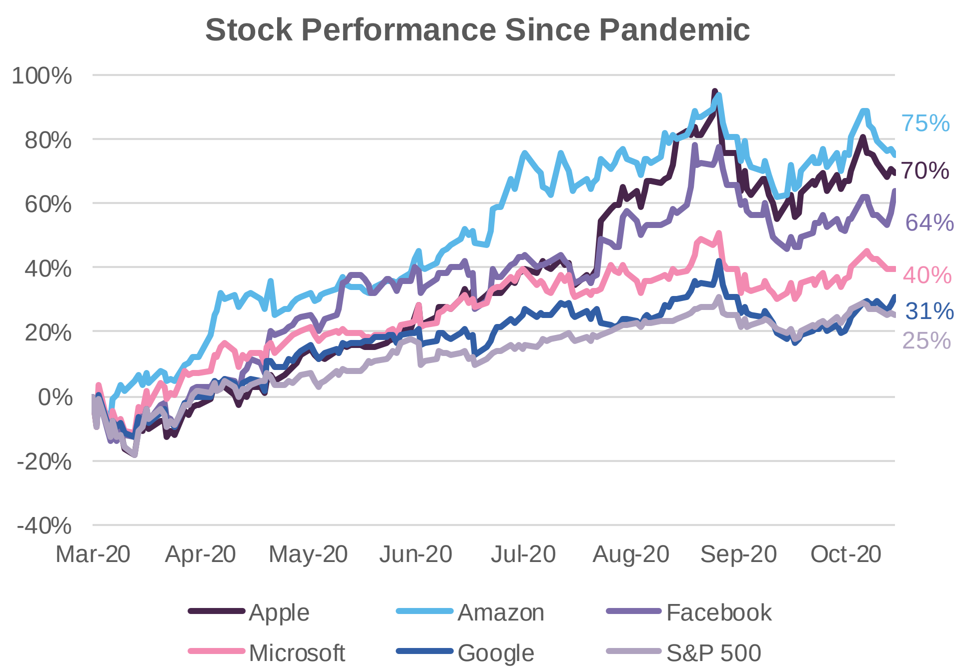
Big Tech is boosting stock market returns

FAMGA Stocks Outperforming Since the Pandemic







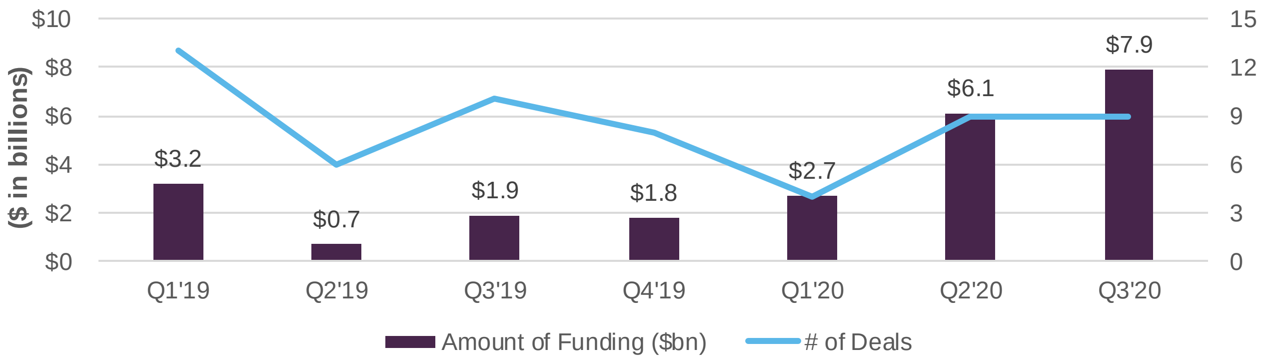
- Top five tech giants FAMGA (Facebook, Apple, Microsoft, Google and Amazon) have been highly profitable
- Increased interest of investors in the technology sector this year has amplified the weight of the FAMGAs in the S&P 500 Index to a record high of 25%, showing 65% increase from their weight three years ago
- FAMGA stocks have been outperforming the overall market since the COVID-19 outbreak was declared a pandemic on March 11, as consumers continue to spend more time and money online
  - The growth has been fueled by a boost in secular trends (such as cloud spending and e-commerce) that continue to be expedited by the pandemic. Consequently, the companies are expected to continue to capture an increasing share of their respective markets

Source: S&P Dow Jones Indices website

Big Tech continues to invest amid the pandemic

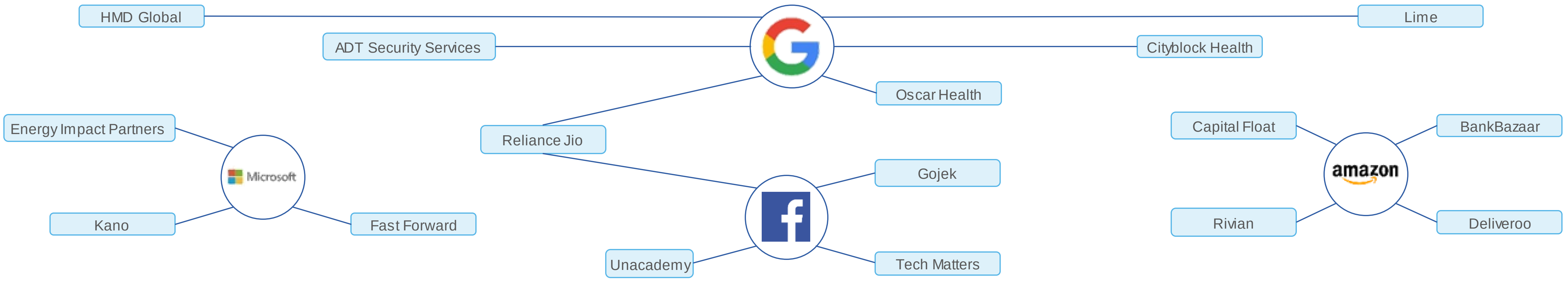
FAMGA’s Recent Investments Amid the COVID-19 Pandemic

Equity Investments / Acquisitions with FAMGA Participation



- A third of the investments made by big tech companies in the past six months were in India-based companies
  - Alphabet, **Google’s** parent company, has made the most investments among the FAMGA cohort since the start of the pandemic. The company has participated in six deals since March, and made most investments (4 rounds) in Q3 2020
  - In April, **Facebook** invested $5.7B for a 10% stake in Reliance Jio, three months before Google’s investment into the company
  - Two of **Amazon’s** 2020 investments were also in India-based companies. Since the declaration of the pandemic, the e-commerce giant has participated in a $3.8M Series D tranche to loan and insurance policy aggregation platform BankBazaar and a $15M Series E to SMB lender Capital Float

Big Tech Investments Amid the Covid-19 Pandemic



Source: CB Insights

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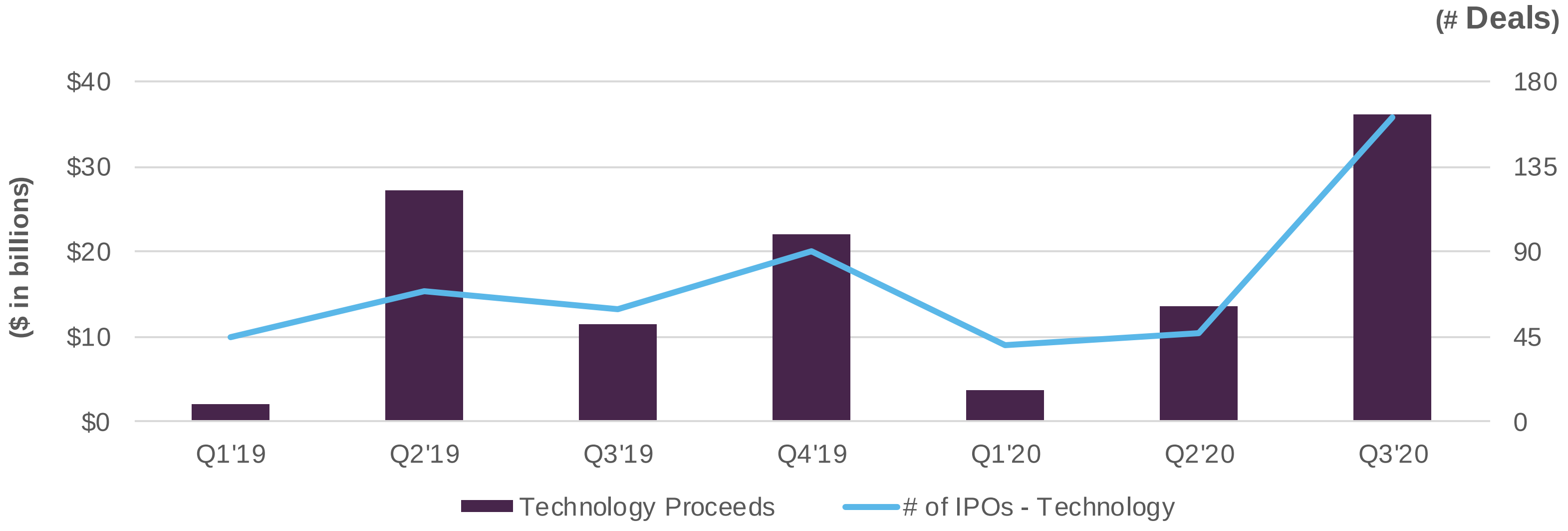
Surge in IPO activity in tech in Q3 2020

Tech IPO Activity



- Globally, the technology sector raised ~$54B through 210 IPOs in 2020 YTD
  - Q3 2020's largest IPO by proceeds was that of Semiconductor Manufacturing International Corp., which raised $7.5B
  - Companies are choosing to go public to increase their capital base for future investments, as well as to remain resilient against a potential next wave of the pandemic
  - Some of the recently listed 'new economy' companies have witnessed strong valuations, giving positive signals to other potential IPO candidates to complete their transactions in the quarters ahead

Source: EY Global IPO Trend Report

SMIC

SMIC is China's biggest contract manufacturer of chipsets. It raised $7.5B in an IPO on July 06, 2020, marking the country's biggest listing in a decade

snowflake

Snowflake, a New York-based cloud data warehouse vendor, raised $3.4B in an IPO on September 15, 2020. Valued at $70B, it is the biggest software IPO ever

asana

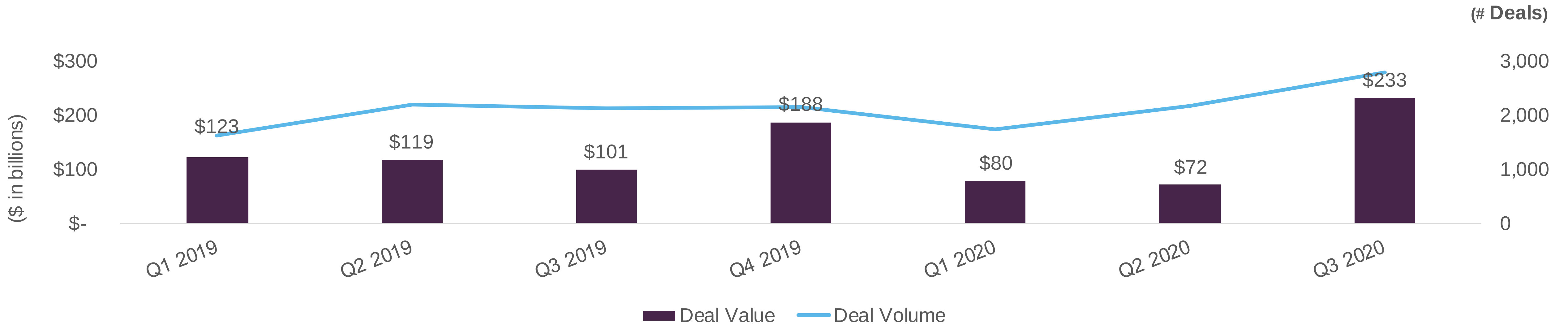
Asana, a provider of enterprise task management and collaboration software, valued at $4B, filed for a public stock listing with the US regulators in September 2020

sumo logic

Sumo Logic, a California-based firm that specializes in machine data, announced listing on September 17, 2020 and had valuation of $2.65B

Tech M&As keep up amid the pandemic

Global High Technology M&A Deals



Source: Refinitiv

- Tech M&As had their best quarter and recorded about $233B worth of deals in Q3 2020. Tech deals are expected to increase, as companies seek technological solutions to challenges posed by COVID-19
- PE firms, with high levels of dry powder, accounted for c.15% of all M&A activity in YTD 2020
  - Largest deals included Blackstone acquiring a majority stake in Ancestry.com from US PE Silver Lake for $4.7B and CDR agreeing to pay $4.7B for software group Epicor

Deal prices are less affected than expected

Currently, there is no pressure on transaction multiples from public markets

Valuations look sustainable, based on the recent earnings growth and low interest rate environment

Software assets are emerging in terms of value

Software assets with a high share of recurring revenues and sound margins have proven to preserve more value than other IT segments

Scarcity of high-quality assets

Increased investor demand for high-quality assets that are expected to come out of the crisis almost unaffected is driving the valuation of premium assets

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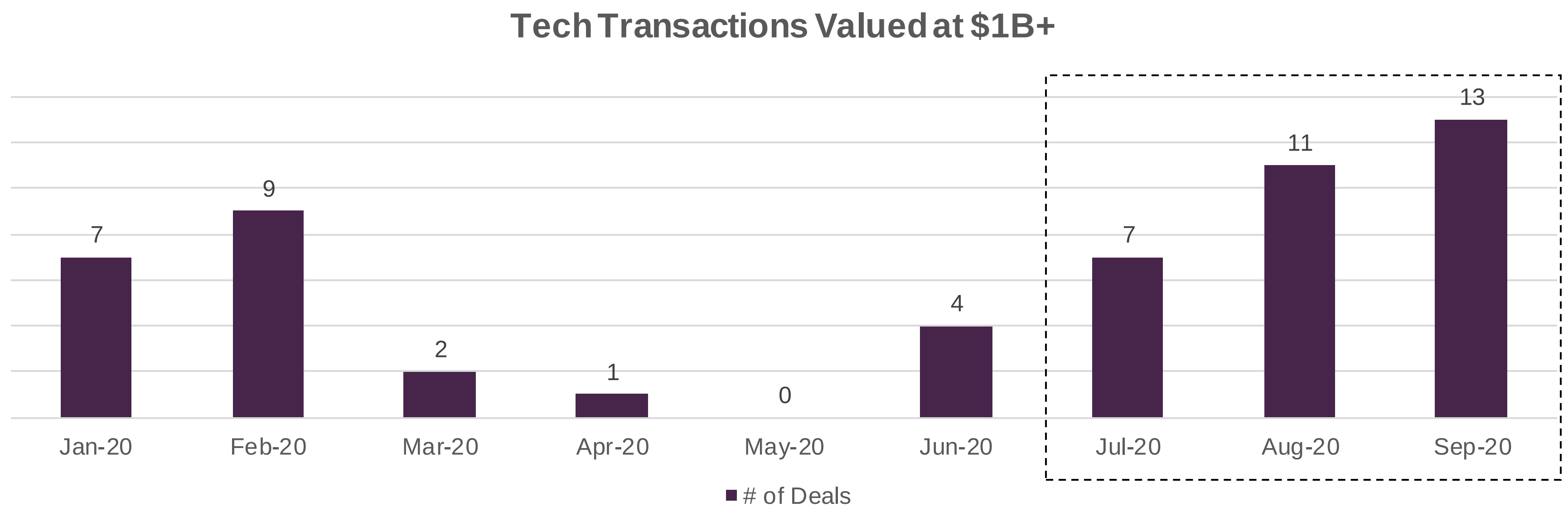
Surge in mega deals in tech sector

Technology Mega Deal Activity in Q3 2020



- In Q3'2020, 21 mega deals announced worth a combined US$256 billion, each valued at US$5 billion and above, with August being the month for strong deal flow in terms of value
  - In August, tech sector accounted for ~27% of global M&A activity, with six of the 10 largest deals were from tech sector targets only
- PE has been active in Q3'2020 as well with majority of the deals occurring in August

Source: Refinitiv

NVIDIA ARM

In September 2020, Chipmaker Nvidia acquired UK-based chip designer Arm, for $40B, creating world's premier computing company for the age of AI

Roper Technologies Vertafore

In August 2020, Roper Technologies announced to acquire Vertafore, a SaaS solutions provider for (P&C) insurance industry, in a deal worth $5.35B

AVEVA OSIsoft

In August 2020, British industrial software provider Aveva Group acquired SoftBank-backed peer OSIsoft for an enterprise value of $5B

Hg VISMA

In August 2020, European software investor Hg announced plans to invest $2B in Norwegian software company Visma Group, valuing the business at an enterprise value of $12.2B

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Predictions for Q4 2020

Factors Affecting Tech Sector

Uncertainty around the pandemic makes tech companies a safe haven for investors

- Tech companies are likely to remain attractive for investment
  - Digitization of business, education, and household is likely to continue as the uncertainty around the pandemic persists
  - Solid fundamentals and resilience of tech companies, vis-à-vis slower recovery of other sectors makes them a safer haven for investors

Very-high valuations may temporarily dampen M&A pace

- While the upbeat deal-making mood is not likely to change totally in Q4 2020, some euphoria is surely going to slow down
  - Very-high valuations will come in the way of deal making
  - Deal momentum is likely to slow down as corporates analyze the possible impact of the outcome of the US presidential elections

Low interest-rates to keep debt-financed deals alive

- Federal Reserve's plan to keep interest rates very low will continue to drive debt-financed deals, including LBOs and MBOs
  - Lower rates could also steer more investors away from treasuries to the tech sector

Big Tech's market dominance spurs US anti-trust probes

- The US Department of Justice has filed a recent anti-trust case against Google
  - Though it will turn out to be a long process, but it is showing that "Big Tech" are under scanner of the US government

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