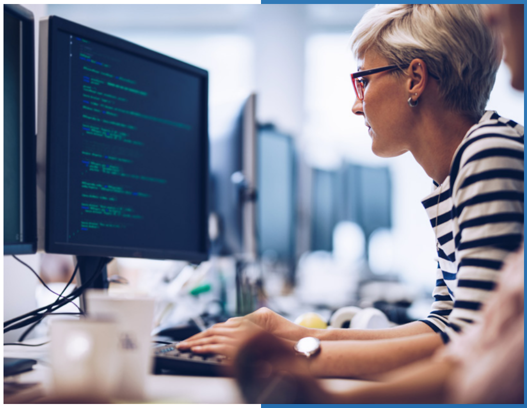
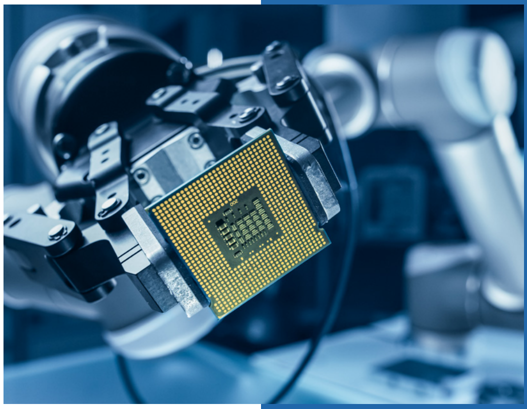
Financing American Innovation:

Private Equity's Role in the Innovation Economy

FEBRUARY 2022





Data provided by PitchBook

Executive summary

For years, the word "innovation" has been synonymous with Silicon Valley and venture capital (VC). But private equity (PE) investors have become effective capital providers to the technology industry. PE firms such as Vista Equity Partners, Thoma Bravo, Silver Lake and Clearlake Capital Group have become industry leaders in the technology sector, and the biggest players in the innovation economy now pay close attention to what they say.

The technology sector is at the forefront of American innovation and is maintaining its international edge thanks to private equity. PE's role goes well beyond capital; PE firms can identify opportunities for technology companies to scale, expand internationally, and help small companies tackle big problems. This report, made in conjunction with PitchBook Data, highlights several examples and success stories. PE has infused new life into hundreds of technology companies, helping smaller companies scale beyond what they could do on their own and helping some of the largest technology companies reinvent themselves to continue competing in the innovation economy.

PE's ability to transform technology companies has been critical during COVID-19. Early in the pandemic, PE sponsors recognized that many companies were not prepared to operate remotely. The technology to do it was already in place, but it was not widely used until COVID-19 struck. PE sponsors helped their own portfolio companies rapidly scale operations, financing the necessary upgrades for potentially long-term changes. PE sponsors also helped the technology companies themselves, which are often founded by brilliant entrepreneurs who sometimes struggle with scale and market adoption. One of PE's best skillsets has been put to use, with little fanfare, over the past two years: recognizing and scaling commercially viable technologies and positioning them to be adopted by many more end users in a short amount of time. While circumstances are still far from ideal, those technologies have saved thousands of jobs and helped ease the burden of working remotely.

PE's position in the innovation economy was considered "new" for many years. Today, firms such as Silver Lake, Vista, and Thoma Bravo are considered some of the most sophisticated minds in technology, maintaining America's lead in the global innovation economy, helping reinvigorate and scale dozens of companies under their lead, and adding jobs to thousands of innovating companies all around the country.

Taking innovation to the next level

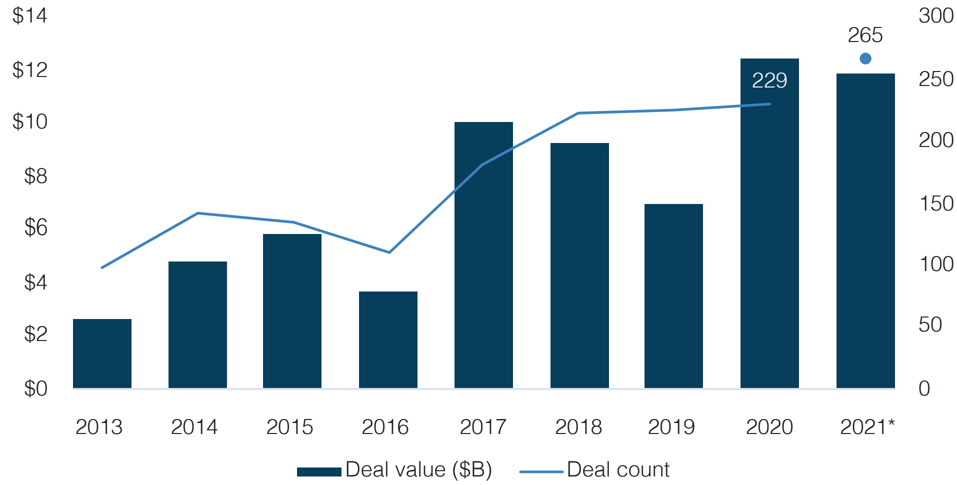
A decade ago, it was uncommon for PE firms to acquire startups. That story is starting to change. Many of today's startups — especially VC-backed software companies — are generating income because they're finding innovative solutions that companies of all sizes can afford. VC helped them get off the ground and become real companies. PE's role is increasingly taking those companies to their next phase of growth.

The story of Marketo is an important one. When NAIC member Vista Equity Partners acquired Marketo in 2016, many in the industry questioned the deal and how much Vista was willing to pay for it. Marketo was losing money at the time, but Vista recognized its potential to reinvent itself in a fast-changing world.Thanks to Vista, Marketo was given a new CEO who had experience in regenerating revenue growth and moving companies into new markets. When Vista took the company private in 2016, it paid almost \$1.8 billion, which many believed was too high a price for a company that was heading downhill. Vista sold Marketo two years later to Adobe for \$4.7 billion, increasing its value by almost \$3 billion. Adobe incorporated Marketo's systems across its business-to-consumer (B2C) and business-to-business (B2B) customer experience platforms and put Marketo's solutions at the heart of its marketing campaigns.

PE investors visit Silicon Valley on behalf of their own portfolio companies, as well. PitchBook data shows that the number of add-ons of VC-backed companies continues to increase.

In these cases, PE firms acquire innovative startups and fuse them with their existing portfolio companies. The practice has become much more common, with more than 200 VC-backed add-ons so far in 2021. Five years ago, only 70 such add-on transactions closed. Going forward, this trend will likely strengthen, and Silicon Valley and other venture ecosystems will provide wellsprings of innovation for

PE buyouts of VC-backed tech startups

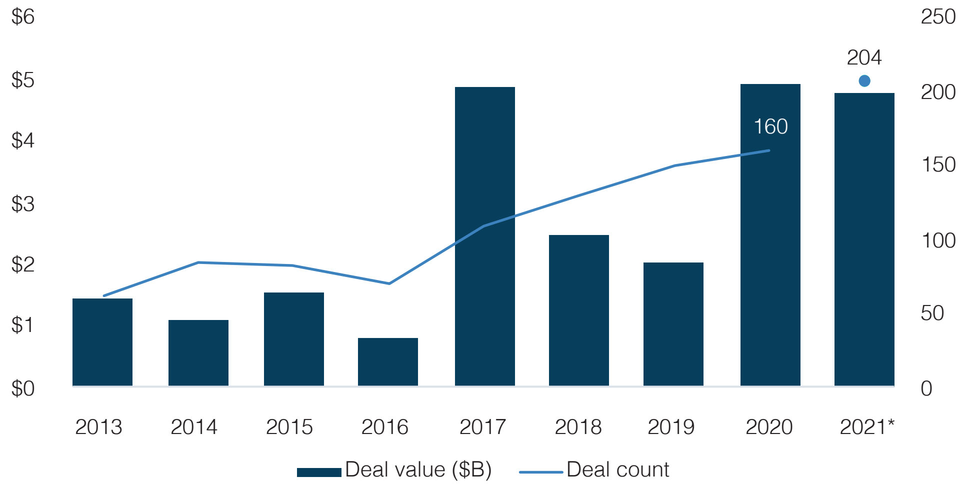


Source: PitchBook | Geography: US
*As of November 10, 2021

PE-sponsored companies.

The software space serves as an excellent example. Most software companies are built to serve specific industries and end users. But at the speed of today's innovation economy, even software companies need to reorient themselves to shifting customer demand. For PE firms that are active in the software sector, VC-backed startups can help platform companies pivot quickly and serve additional customers in a short amount of time. In other cases, PE firms can buy startups with specialties in artificial intelligence (AI) or machine learning (ML) and instantly infuse their own portfolio companies with cutting-edge technologies.

Add-ons of VC-backed tech startups



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Private equity at work

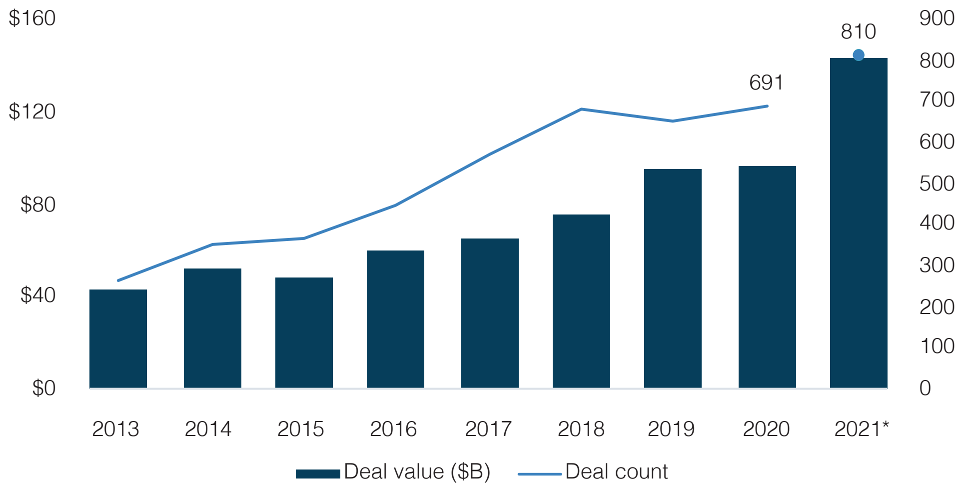
Marketo™ An Adobe Company

NAIC member Vista Equity Partners acquired Marketo in 2016. An underappreciated company at the time, Vista helped grow the company's value by $3 billion in the span of two years. That process started when Vista recruited Steve Lucas as Marketo's new CEO. Lucas was attracted to Vista's approach, from its operational expertise to the best practices Vista implemented once the deal was struck. The partnership also relied on Vista's emphasis on driving innovation and its long-term outlook for the company. New technologies were implemented, driven by AI & ML applications, which allowed Marketo to take calculated risks that eventually paid off. In 2018, Marketo was acquired by Adobe, which incorporated Marketo's technology across its B2C and B2B customer experience platforms.

Fueling the software boom

PE has taken the software industry by storm. In 2021, PitchBook data has tracked over $140 billion in software-related dealmaking, the first time the PE industry has collectively breached the $100 billion barrier. Over 800 software companies have taken in PE funding in 2021, and eventually that number will reach 1,000. Over the past decade, 5,286 software companies have received PE investment. The range of software companies is broad and impacts dozens of sectors in the American economy: workflow software, business & productivity software, database platforms, network management software systems, and financial software platforms, among many others.

PE activity in software companies



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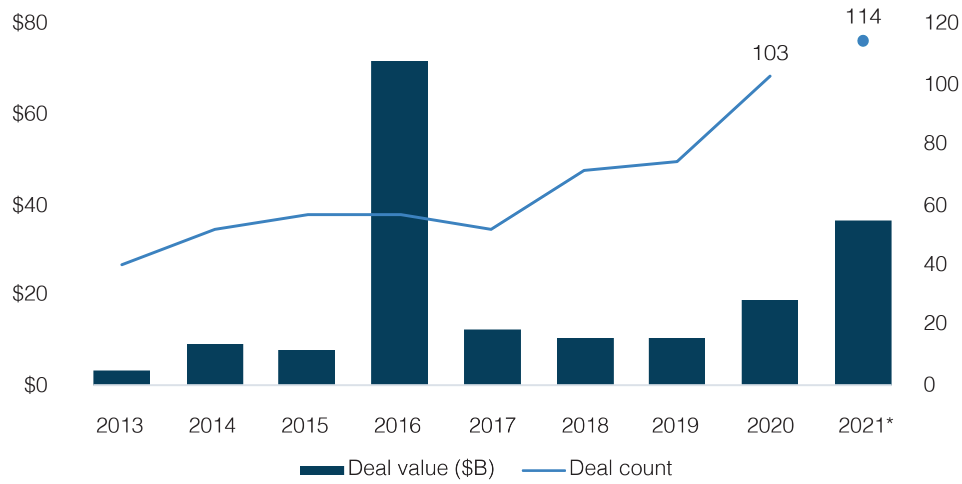
PE's unique skillset in the software industry is helping individual companies expand their offerings, scaling them effectively without imposing extravagant costs on their management teams. PE firms can also help software companies pivot into new markets, an important value-add in a dynamic and innovative industry. The PE playbook often boils down to adding customers at a minimal cost, driving revenue higher, adding new job offerings, and improving balance sheets. Those revenue increases can then finance new innovations and service offerings. Those skills are especially vital in today's world: Under COVID-19, much of life has moved online, and reliable platforms are required to help keep businesses and organizations running smoothly.

Strengthening cybersecurity

Cybersecurity strikes are an increasing part of corporate life. According to the Identity Theft Resource Center, 2021 has already seen more security compromises than all of 2020 combined, with 1,291 incidents through September 30 compared to 1,108 incidents last year. In both years, hundreds of millions of people were potentially impacted. Cybersecurity threats are widespread by sector, with attacks on government organizations, financial firms, healthcare providers, and retail companies, to name a few.

PE investors have become reliable allies for the cybersecurity industry. Over the past two years, over 200 cybersecurity providers have taken PE investment. As investors in the space, PE firms are helping cybersecurity companies innovate and broaden their offerings, opening new doors to other industries and expanding their workforces along the way. The ultimate beneficiaries are the clients of those cybersecurity providers, which require sturdy and reliable security solutions to avoid breaches and a loss of trust from their own customers.

PE activity in cybersecurity companies



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Private equity at work

ENTRUST

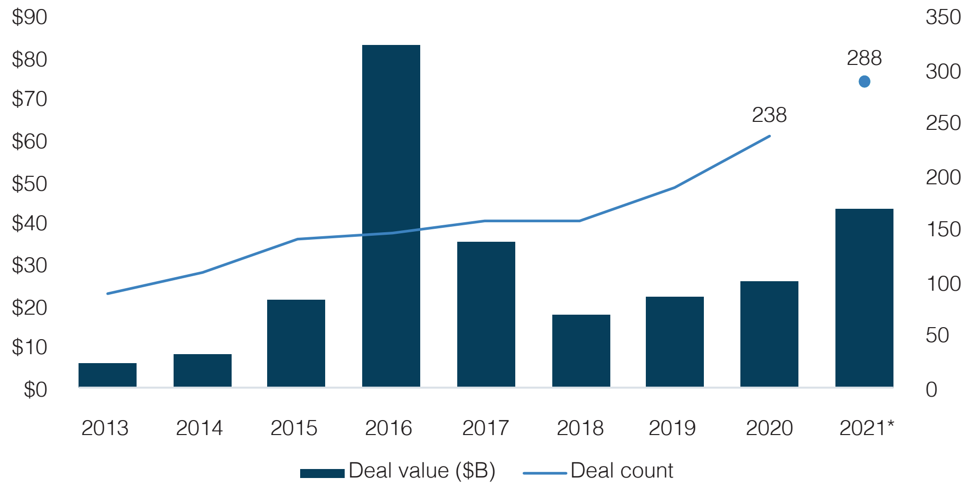
AIC member Thoma Bravo acquired Entrust, a San Francisco-based cybersecurity company, in 2009. Thoma Bravo set high expectations for the company, implementing ambitious financial goals and a long-term strategy for Entrust. By 2012, Entrust had overachieved those goals, with significant improvements in total revenue growth and cloud- and subscription-based growth. Gains aside, Entrust's partnership with Thoma Bravo also resulted in a transformation of the company's intellectual property portfolio, which helped make Entrust into an industry leader in the identity-based security market.

Bolstering IT services

PE has become a major player in the IT services industry, which spans dozens of applications. PE firms have sponsored IT consulting and outsourcing companies for many years. More recently, PE firms are helping cloud computing companies expand their resources and product offerings. PE firms are also helping IT companies focused on remote work solutions, which became a necessity during the pandemic. PE is adept at adding scale to its portfolio companies, and that ability can be translated to systems and information management just as easily.

Over the past decade, PitchBook statistics show almost $300 billion in PE going to IT service providers, including almost $70 billion over the past two years. That capital is used to improve back-end systems, finance new innovations in cloud computing and remote work solutions, and expand the reach of regional data centers. Those improvements ultimately benefit companies of all sizes, including Main Street businesses that rely on cost-effective services while they focus on their own customers.

PE activity in IT services companies



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Private equity at work

AIC member Silver Lake formed Vantage Data Centers in 2010. Silver Lake originally purchased a data center campus in California that had been operated by Intel. Over a seven-year holding period, Silver Lake grew Vantage into a much larger data center provider, turning it into one of the biggest US-based providers in the industry. Under Silver Lake, Vantage grew its Santa Clara, CA data center to a total capacity of 51 megawatts. It was sold to a group of investors in 2017 while building a new Santa Clara facility with 69 megawatts of total capacity.

Private equity at work — Success stories

Idaptive, a California-based identity security provider, was originally part of a company called Centrify. Thoma Bravo bought Centrify in the summer of 2018 and carved out its Identity-as-a-service (IDaaS) business as a new standalone company called Idaptive. Thoma Bravo installed Danny Kibel as Idaptive's first CEO after Kibel helped develop Centrify's IDaaS platform in its Engineering and Operations department. Kibel's role with Idaptive was to create a market-leading IDaaS business and accelerate innovation within the standalone company. Two years after it was formed, Idaptive was sold to CyberArk, a public software company that specializes in privileged access management.

Xactly is a California-based software company that helps its clients develop compensation plans. It went public in 2015, but Xactly struggled to grow under the constant scrutiny of public investors. The company's founder and CEO, Chris Cabrera, sought out a PE sponsor to help Xactly rethink its growth initiatives. He met with Vista Equity Partners, which encouraged Xactly to look beyond traditional growth metrics and focus on other factors to boost its long-term initiatives. Vista took the company private in 2017 and recruited senior professionals to join the cause. Vista also made introductions to executives and experts who were working for other Vista portfolio companies, creating a cross-pollination effect that boosted innovation for Xactly. Still a Vista portfolio company, Xactly has grown its workforce by the hundreds.

Accruent, a Texas-based software company that services real estate and facilities management clients, has transformed itself under several PE sponsors, including NAIC member Vista Equity Partners, Virgo Capital, and AIC members TA Associates and Genstar Capital. Its PE sponsors recruited several veterans of the industry into existing and newly created positions to help it scale. Accruent helps companies of all sizes contain one of their biggest expenses: their real estate and facility costs. Accruent now serves more than 10,000 clients around the world. Its PE sponsors brought Accruent into the healthcare industry, and its real estate software platform is now used by more than half of all hospitals in the US. The company's cost-effective solutions allow its clients to improve productivity and stay on top of industry compliance, while cutting costs that can be used to hire more employees and finance more innovation down the road.

Private equity at work —Upgrading portfolio company operations

Behind the scenes, PE firms routinely use their own funds to upgrade their portfolio companies' tech operations. During COVID-19, PE firms redoubled their efforts, helping portfolio companies of all shapes and sizes ease their workforces into remote environments. That cushioned the blow for millions of employees to continue working efficiently and helped their employers minimize layoffs over the past two years. While PE's efforts are more obvious today, sponsors routinely helped upgrade their portfolio companies before the pandemic, and they will continue their efforts once COVID-19 has fully passed.

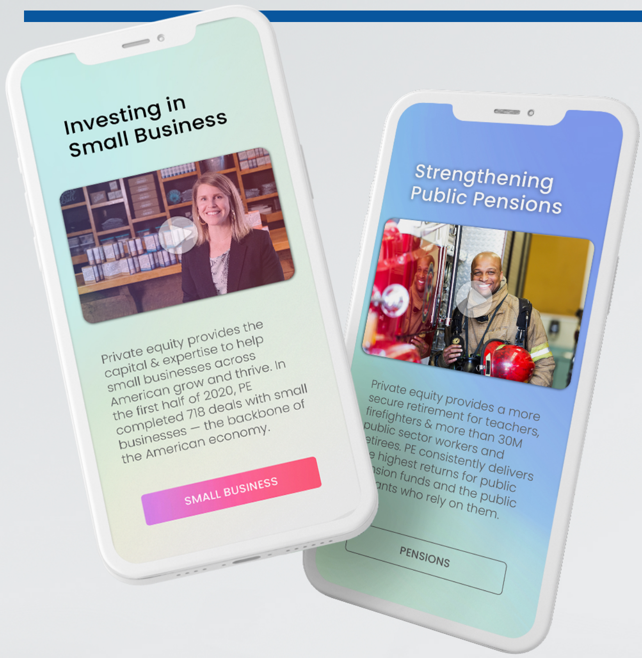
For example, investors focused on healthcare or consumer companies seek out industry-specific solutions and purchase them for every company in their portfolios. The cybersecurity needs of healthcare companies can be different than the cybersecurity needs of consumer companies. PE firms are focused on improving every aspect of a portfolio company that they can, including behind-the-scenes improvements that often go unnoticed. And because they can purchase those services at scale and across entire portfolios, firms can often do it at a discount, ultimately benefiting the companies themselves.

An entire cottage industry has developed around meeting those needs. Today there are dozens of "private equity consultants" who can help PE firms assess the needs of their portfolio companies and match them with the best vendors available. Those services ultimately find their way to the chief technology officers (CTOs) of PE-backed companies. PE firms work closely with CEOs and CFOs on where their companies are going, but they work just as closely with portfolio company CTOs on ways to modernize their operations. That includes software upgrades, improvements in cloud computing, and incorporating dozens of other solutions to save their companies time and money.

PRIVATE EQUITY
INVESTING IN AMERICA

From urban to rural and everywhere in between, private equity is making a positive impact across America and investing in every community to:

- Back small businesses
- Support good-paying jobs
- Boost the American economy
- Strengthen public pensions



The American Investment Council (AIC) is an advocacy and resource organization established to develop and provide information about the private investment industry and its contributions to the long-term growth of the U.S. economy and retirement security of American workers. Member firms of the AIC consist of the country's leading private equity and growth capital firms united by their successful partnerships with limited partners and American businesses.

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