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2008 Review and
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We welcome the opportunity to have a more detailed discussion of the Commercial Technology market.

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IT Services M&A— 2008 Review and Expectations for 2009

By [Erin Lucien](#) and [Gretchen Guandolo](#), KippsDeSanto & Co.

IPO and M&A Activity in 2008...What a Ride

It was the best of times, it was the worst of times... 2008 was a year for the record books. Over the past 12 months, our country witnessed a landmark presidential election as well as one of the worst economic crises in recent history. With the credit markets eroding, the government taking an unprecedented role in the private sector, industry moguls of Wall Street disappearing overnight and other once pillars of strength in our nation's economy lining up for government bailouts, the financial markets have been on a roller coaster of a ride. Despite moderate performance in the first half of the year, the NASDAQ began its steady and steep descent in September to end the year down nearly 40%. The U.S. IPO market closed their doors leaving a wake of companies unable to access the public markets for liquidity. Only 64 companies went public in 2008, down over 75% from the 281 IPOs in 2007. Technology companies found the IPO market an unlikely path to liquidity in 2008 with only five technology IPOs compared to 59 in 2007. The M&A markets were more receptive for those seeking an exit, though deal activity was also down from prior levels. Technology M&A transaction volume fell approximately 10% in 2008 over 2007, while the average deal value declined over 30%. The larger decline in value illustrates both the valuation contraction broadly occurring across the technology market as well as the movement toward small to mid-market transactions in 2008 - a trend we expect to continue in 2009.

Federal IT Services Remains a Beacon of Light

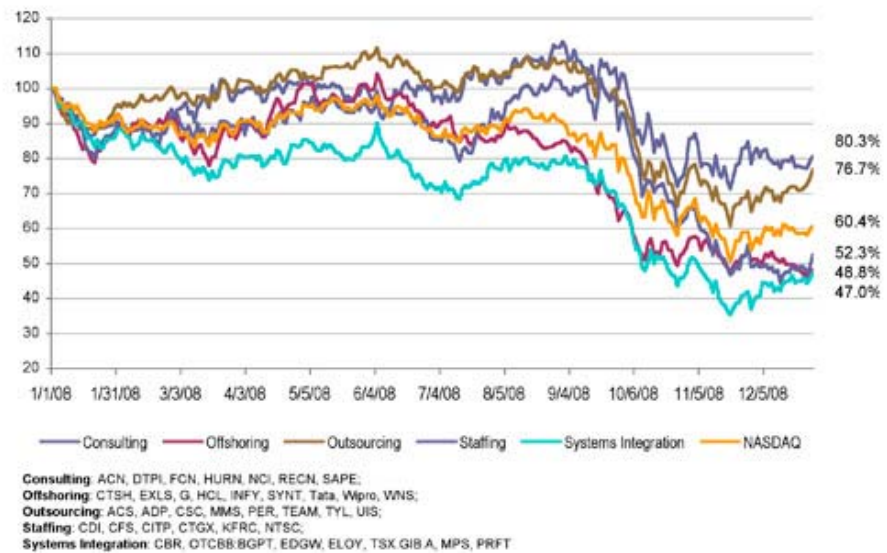
While technology M&A activity has certainly been impacted by the broader issues facing the U.S. and global economy, deals are still closing and quality targets with solid fundamentals in attractive markets continue to garner healthy valuations. Within the IT services market, federal IT services M&A has been a bright spot with over 100 transactions announced in 2008. Stanley Inc.'s \$170 million acquisition of Oberon Associates, Inc.¹, a leading provider of biometrics systems engineering, intelligence operations support and communications engineering services to the federal government, is an excellent example of buyers seeking access to high-growth, next generation technologies that are likely to benefit from future federal spending. Moreover, companies supporting the national intelligence community continue to command strong M&A interest. Federal IT services companies outperformed the NASDAQ by approximately 45% in 2008. However, while the Federal IT services index outperformed the NASDAQ and the commercial IT services indices, this sector has not been immune to value contraction. Federal IT services companies' median LTM revenue and EBITDA multiples were down approximately 15% and 20%, respectively at the end of 2008 compared to 2007. While valuations among Federal IT services companies are also under increasing pressure, the Federal IT services M&A market continues to be an active arena with buyers increasingly focused on adding specific capabilities in light of the new administration's anticipated funding initiatives.

Commercial IT Services - More of a Mixed Bag

Commercial IT Services² firms saw strong demand in the first half of the year, but as the economy

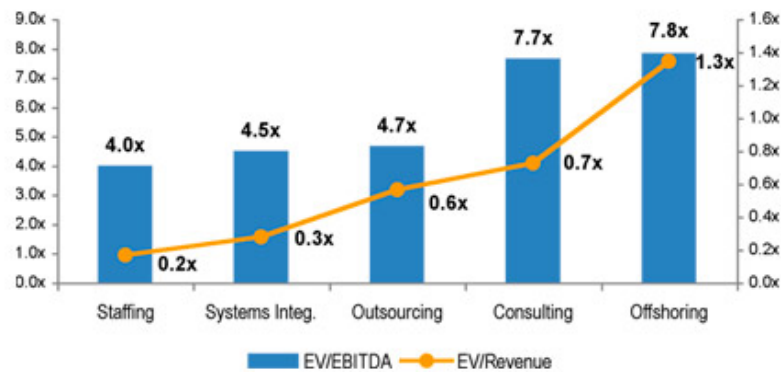
weakened, clients sought to rein in spending. Many vendors began to experience increased pricing pressure, new approval processes and decision delays with the financial services market being especially hard hit. The trading performance of KippsDeSanto's IT Services indices were mixed compared to the broader NASDAQ performance in 2008. The IT Consulting and Outsourcing indices outperformed the NASDAQ for the year, with IT Consulting and Outsourcing declining 20% and 23% for the year compared to the steeper 40% decline in the NASDAQ. The Offshoring, IT Staffing and Systems Integration indices did not fare as well; all underperformed the NASDAQ in 2008. In late 2008, publicly traded IT services companies broadly began announcing downward revisions to revenue and earnings in anticipation of the headwinds expected in 2009 and added foreign exchange implications of the strengthening U.S. dollar to their list of market challenges.

*Commercial IT Services Relative 1-year Public Pricing Performance
(AS OF 12/31/08)*



Global spending on IT Services and Outsourcing by governments and businesses is expected to decline in 2009 before posting positive growth again in 2010. Purchases in this category are expected to fall 3% in 2009 to \$484 billion before rising 9% in 2010³. Service providers, such as IT consulting and outsourcing firms who have differentiated, value added offerings, including those that address their customers' need to minimize risk and reduce operational costs, are expected to outshine their peers. The shocking, recent news of Satyam's bogus cash balance and fraudulent accounting is not expected to detract from demand for outsourcing over the long term, particularly given the current focus on cost containment. However, in the coming months, outsourcing vendors should anticipate increasing scrutiny and due diligence as clients seek to reevaluate vendor risk. Long term, we believe that Tier I outsourcing vendors, such as Infosys, Cognizant, Perot, Accenture and IBM will benefit from the collapse of Satyam by giving outsourcing clients renewed confidence in their vendors and gaining revenue and market share in the process.

Public Company Pricing Multiples (AS OF 12/31/08)



An Interesting Year for M&A

M&A played an important and interesting role in the Commercial IT Services market in 2008. We have tracked over 160 U.S. IT Services transactions with IT consulting and systems integration companies comprising the majority of announced deals. Strategic acquirers accounted for over 90% of all transactions in 2008 with financial buyers playing a much less active role, a trend we expect to continue in 2009 in light of the current funding environment and credit markets.

The blockbuster deal of the year award goes to HP's \$13.9 billion acquisition of EDS, announced in May. This acquisition more than doubles the size of HP's services revenue and catapults it to one of the top two IT services vendors in the world behind IBM. In the IT Offshoring world, Tata Consultancy closed its acquisition of Citigroup Global Services Limited from Citigroup, Inc. on December 31st for approximately \$512 million in cash, broadening its portfolio of technology and BPO services in the global banking and financial services markets. Finally, we cannot speak of noteworthy transactions without mentioning HCL Technologies' acquisition of Axon Group plc. After a long pursuit of the SAP focused business transformation consultancy, HCL completed the acquisition of Axon Group for nearly \$763 million in mid-December. Highlighted deals from 2008 include:

Notable 2008 Transactions

Announce	Close	Buyer	Seller	Description	EV	EV/Revenue	EV/EBITDA
11/30/08	11/30/08	Kforce Government Solutions, Inc.	dNovus RDI	Provides large network design, implementation, operations, and maintenance.	\$38.0	1.19x	NA
10/08/08	12/31/08	Tata Consultancy Services Limited	Citigroup Global Services Limited	India-based captive business processing outsourcing (BPO) arm of Citi.	531.8	NA	NA
09/26/08	12/15/08	HCL Technologies Ltd.	Axon Group plc	SAP focused business transformation consultancy, designs, implements, and supports solutions to business issues faced by organizations.	762.8	1.66x	10.2x
08/06/08	08/06/08	Sapient Ltd.	Derivatives Consulting Group	Provides operational support for derivatives processing and advisory services.	60.7	0.70x	NA
07/24/08	07/24/08	Rosetta Marketing Strategies Group	Brulant, Inc	Interactive marketing agency working with top brands in the Retail & Consumer Goods, Financial Services and Hospitality industries.	NA	NA	NA
06/03/08	07/17/08	Deloitte LLP	Solbourne Computer, Inc.	Provides enterprise solutions based on Oracle's E-Business Suite and PeopleSoft Enterprise applications.	NA	NA	NA

05/13/08	09/11/08	Hewlett-Packard Co.	Electronic Data Systems Corporation	Provides a range of information technology and business process outsourcing services worldwide.	13,900.0	0.62x	5.7x
04/01/08	04/01/08	ABRY Partners, LLC	Hosted Solutions, LLC	Data center operator and managed services provider.	140.0	NA	NA
04/01/08	04/01/08	EMC Computer Systems Ltd.	Conchango plc	Provides business consultancy and systems integration services in the United Kingdom.	63.0	1.27x	14.0x
03/04/08	04/26/08	Brocade Communications Systems, Inc.	Strategic Business Systems, Inc.	Provides IT infrastructure design, integration, and operations services to non-profit and government entities.	NA	NA	NA
01/09/08	01/09/08	Affiliated Computer Services Inc	Syan Holdings Limited	Provides information technology outsourcing services.	60.0	0.80x	NA

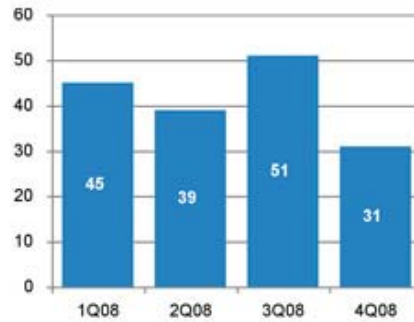
What to expect in 2009

In 2009, we expect to see the continuation of themes from the latter half of 2008 as well as new themes and trends taking hold.

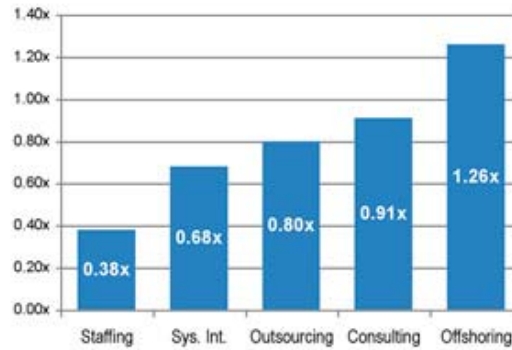
- **Caution prevails - middle market activity reigns:** In conversations with buyers across both services and software markets, the tone continues to be one of "proceed with caution." The appetite for M&A does not seem diminished, but the appetite for risk certainly has. This dynamic is leading acquirers to target smaller transactions that add a particular competency or expertise without adding tremendous execution or financing risk. The limited availability of financing and resulting need to use cash on hand as acquisition currency further supports/accelerates the movement towards smaller deals.
- **Cash-rich buyers in the catbird seat:** Again, the impact of the debt crisis reverberates across the M&A markets, leaving those companies with solid cash on their books in a stronger position than ever. We expect to see cash as the predominant form of deal currency in 2009 with creative financing, such as seller notes being increasingly used.
- **Heightened interest in IT services from software and hardware vendors:** In 2008, we saw several transactions highlighting the desire of traditional software and hardware vendors to strengthen their services offering and expect this to continue in 2009. EMC's acquisition of Conchango plc, a UK-based consulting and systems integration firm, for \$63 million is one such example. Dell kicked off 2009 with a \$12 million acquisition of several divisions of Allin Corp, an IT consulting firm, amid rumors that it may be eyeing another large IT services transaction.
- **Leveraging the need to do more with less:** Fueled by considerable pressure to reduce expenditures, companies are increasingly seeking to gain additional value from existing investments, whether they are in Microsoft, Oracle or SAP systems and are turning to service providers to help them accomplish this. While M&A interest for SAP integrators has traditionally been strong, we are seeing increasing interest in Microsoft (RCM Technologies' acquisition of NuSoft Solutions, a Microsoft Gold-Certified partner) and Oracle technologies (TITAN Technology Partners' acquisition of Pinnacle Group Worldwide).
- **IT services spending follows "hot" areas of the IT Sector:** Service providers with competencies in security, compliance/risk management, cloud computing and infrastructure management are expected to see stronger demand while healthcare, energy, pharma and the U.S. government are anticipated to be market leading verticals.
- **Valuation gap to narrow in 2009:** The equilibrium in valuation expectations has not fully materialized between buyers and sellers, as the events of the latter part of 2008 continue to shake out. We saw many deals stall as the valuation expectations widened in the second half of 2008. We expect to see the valuation expectation gap narrow between buyers and sellers in the coming

year.

2008 Commercial IT Services M&A Volume



2008 Median M&A Revenue Multiples by Sector



¹ KippsDeSanto & Co. acted as financial advisor and Cooley Godward Kronish acted as the legal advisor to Oberon Associates, Inc. in this transaction.

² KippsDeSanto defines Commercial IT Services to include IT Consulting, Outsourcing, Systems Integration, Offshoring and IT Staffing.

³ Forrester Research, "Global IT Market Outlook: 2009", January 12, 2009.

Disclaimer

The information and opinions in this report were prepared by KippsDeSanto & Co. and the information herein is believed to be reliable and has been obtained from and based upon public sources believed to be reliable. KippsDeSanto & Co. makes no representation as to the accuracy or completeness of such information. Opinions, estimates and analyses in this report constitute the current judgment of the author as of the date of this report. They do not necessarily reflect the opinions of KippsDeSanto & Co. and are subject to change without notice.