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# WAS THIS CLOUD GROWN ORGANICALLY?

Kara Marciscano — Associate, Research

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The Software & Services industry can be divided into two factions: the cloud software providers and the traditional software providers.

There is widespread agreement among industry stakeholders that software deployment via cloud, otherwise referred to as providing [Software as a Service \(SaaS\)](#), is the preferred business model.

Software companies and their shareholders tend to particularly align in support of the SaaS subscription-based revenue model. While traditional software companies derive revenue from single, large and upfront transactions, cloud SaaS companies employ a recurring revenue model with smaller and more frequent transactions. The SaaS model is preferred, which can result in a more predictable, annuity-like revenue stream.

Traditional software company Citrix Systems (CTXS) recently announced a strategic transition to a subscription-based revenue model. Its CEO discussed a few commonly cited reasons for the shift to cloud<sup>1,2</sup>:

**Transparency**—*“...the strength that we’re seeing in subscription bookings serves to improve our predictability and certainly accelerate our growth in future periods.”*

**Faster Growth**—*“...the fastest-growing part of the business is pure SaaS.”*

**Client Demand**—*“There are secular changes going on in networking driven by the adoption of cloud more than anything else....We’ve seen...a more pronounced move to software versus hardware. And that’s simply because customers are looking for more flexibility, more choices in a way that they deploy their capabilities.”*

Traditional software companies are pursuing the cloud model both organically, like CTXS, and inorganically through mergers and acquisitions (M&A).

Meanwhile, the intensifying competition within the Software & Services industry has driven consolidation among SaaS providers, as well as private takeouts.

As evidenced by M&A activity within the [BVP Nasdaq Emerging Cloud Index \(EMCLOUD\)](#), SaaS companies have been acquired by traditional software companies, cloud peers and private equity firms at premium valuations.

Since EMCLOUD’s inception in October 2018, there have been 11 transactions announced at an average deal premium<sup>3</sup> of ~40%. Notably, all but two of the transactions involved an EMCLOUD constituent as the M&A target.

Announcement Date	Target	Acquirer	Deal Value (\$bn)	Deal Value (\$ per share)	Undisturbed Price (\$ per share)	Deal Premium (% per share)	Deal Multiple Price-to-Forward Sales	Undisturbed Multiple Price-to-Forward Sales	Undisturbed Price Date	Deal Status
12/17/2019	<b>LogMeIn, Inc.</b>	Francisco Partners (Private Equity)	\$4.3	\$86.05	\$68.70	25%	3.2x	2.6x	9/18/2019	Pending
12/4/2019	<b>Instructure Inc</b>	Thoma Bravo LLC (Private Equity)	\$2.0	\$47.60	\$40.42	18%	6.1x	5.4x	10/27/2019	Pending
11/11/2019	<b>Carbonite Inc</b>	Open Text Corp	\$1.4	\$23.00	\$12.93	78%	1.5x	0.8x	9/5/2019	Pending
8/22/2019	<b>Carbon Black Inc</b>	VMware Inc	\$2.1	\$26.00	\$18.70	39%	7.1x	5.0x	8/8/2019	Completed
6/12/2019	<b>Medidata Solutions Inc</b>	Dassault Systemes SE	\$5.8	\$92.25	\$78.87	17%	7.0x	5.9x	4/18/2019	Completed
6/10/2019	Tableau Software Inc	<b>salesforce.com Inc</b>	\$15.7	~\$175.00	\$125.21	40%	10.5x	7.5x	6/7/2019	Completed
2/4/2019	<b>Ultimate Software</b>	Hellman & Friedman (Private Equity)	\$11.0	\$331.50	\$277.83	19%	7.3x	6.1x	2/1/2019	Completed
12/24/2018	<b>MINDBODY Inc</b>	Vista Equity Partners LLC (Private Equity)	\$1.9	\$36.50	\$21.72	68%	5.9x	3.5x	12/21/2018	Completed
11/11/2018	<b>Apptio Inc</b>	Vista Equity Partners LLC (Private Equity)	\$1.9	\$38.00	\$24.85	53%	6.5x	4.3x	11/9/2018	Completed
10/15/2018	<b>SendGrid Inc</b>	<b>Twilio Inc</b>	\$2.0	\$36.92	\$30.93	19%	10.1x	8.5x	10/15/2018	Completed
10/12/2018	Rentlytics Inc	<b>RealPage Inc</b>	\$0.1	NA	NA	NA	NA	NA	10/11/2018	Completed

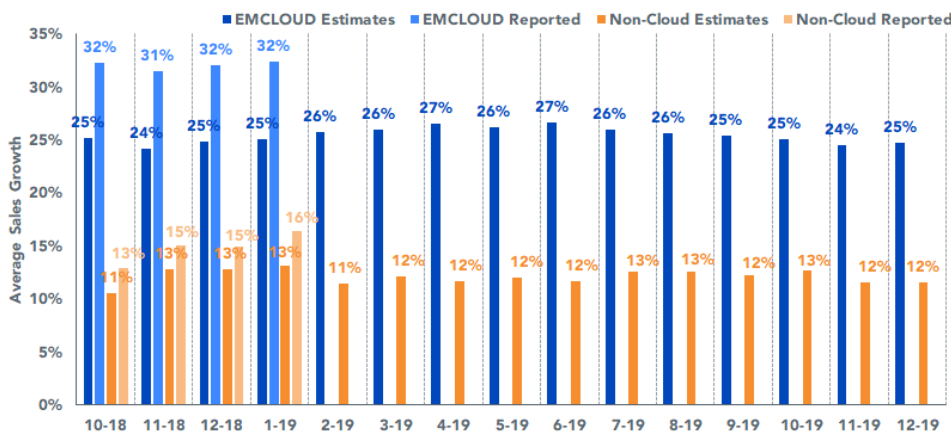
Sources: WisdomTree, Bloomberg, as of 12/31/19. The above figure summarizes announced merger and acquisition transactions involving constituents of the BVP Emerging Cloud Index (EMCLOUD) since inception on 10/2/18 through 12/31/19. EMCLOUD constituents are designated with highlighted borders. Past performance is not indicative of future results. You cannot invest directly in an index. Weights subject to change. Undisturbed price (\$ per share): the closing price of an equity security on the date immediately prior to rumors of M&A activity. Deal premium (\$ per share): the excess price paid by the acquiring company and the market price of the target company. Deal multiple price-to-forward sales: Price paid by acquirer for target company divided by consensus estimated sales growth for the target company over the forward 12 months. Undisturbed multiple price-to-forward sales: Undisturbed market price of the target company by consensus estimated sales growth for the target company over the forward 12 months. Undisturbed price date: the date immediately prior to the first rumor of M&A activity involving a security.

For definitions of terms in the chart, please visit our [glossary](#).

Acquirers of SaaS businesses are paying a premium for both expected and realized growth.

Consensus sales growth estimates for cloud SaaS companies are consistently double those of traditional non-cloud software companies; the average sales growth expectation for cloud has been ~25% as compared to ~12% for traditional software. More importantly, reported sales growth for cloud companies has exceeded consensus forecasts<sup>4</sup> at a wider margin than non-cloud companies.

### Consensus 12-Month Forward Sales Estimates vs. Reported



Sources: WisdomTree, FactSet, as of 12/31/19. Average sales growth estimates for the BVP Nasdaq Emerging Cloud Index and the non-cloud basket calculated as the average growth rate of forward 12-month consensus sales estimates relative to reported sales over the trailing 12-month sales across companies held in each basket at the indicated date. Reported sales growth calculated as the average year-over-year percentage change in reported trailing 12-month sales for the companies held in each basket at the indicated date. Please see disclosure at the bottom of this writing for the list of companies included in the non-cloud basket. Past performance is not indicative of future results. You cannot invest directly in an index.

### Gaining Exposure to Cloud M&A

This year, WisdomTree launched the [WisdomTree Cloud Computing Fund \(WCLD\)](#), which seeks to track the yield and

performance, before fees and expenses, of the BVP Nasdaq Emerging Cloud Index (EMCLOUD).

EMCLOUD leverages the expertise of Bessemer Venture Partners (BVP), a leading early-stage investor in cloud-based businesses. BVP sets the investment parameters for selecting eligible cloud company constituents within EMCLOUD's investment methodology. The constraints determined by BVP provide a differentiated overlay to company selection with a focus on identifying emerging companies with rapid growth characteristics. BVP's investment criteria also target companies that are predominantly deriving revenue through the cloud subscription model. These constraints provide "pure" exposure to the cloud software industry while avoiding exposure to traditional software businesses that have been slow to adapt to the SaaS industry standard.

We believe the disruptive, organic growth and the compelling economics of the SaaS revenue model are key reasons why many cloud businesses have become acquisition targets.

To gain exposure to a basket of cloud SaaS businesses with the potential for heightened M&A activity, investors should consider adding WCLD to their portfolio.

<sup>1</sup>Sources: WisdomTree, FactSet, Citrix Systems, Inc. Q2 2019 Earnings Call.

<sup>2</sup>Citrix System (CTXS) is not held in WCLD as of 12/31/19.

<sup>3</sup>Deal premium/discount is the difference between the price paid by the acquiring company and the market price of the target company. A large deal premium is typically viewed positively by shareholders of the target company.

<sup>4</sup>Source: FactSet, as of 12/31/19.

#### **Important Risks Related to this Article**

There are risks associated with investing, including possible loss of principal. The Fund invests in cloud computing companies, which are heavily dependent on the Internet and utilize a distributed network of servers over the Internet. Cloud computing companies may have limited product lines, markets, financial resources or personnel and are subject to the risks of changes in business cycles, world economic growth, technological progress and government regulation. These companies typically face intense competition and potentially rapid product obsolescence. Additionally, many cloud computing companies store sensitive consumer information and could be the target of cybersecurity attacks and other types of theft, which could have a negative impact on these companies and the Fund. Securities of cloud computing companies tend to be more volatile than securities of companies that rely less heavily on technology and, specifically, on the Internet. Cloud computing companies can typically engage in significant amounts of spending on research and development, and rapid changes to the field could have a material adverse effect on a company's operating results. The composition of the Index is heavily dependent on quantitative and qualitative information and data from one or more third parties, and the Index may not perform as intended. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

The non-cloud baskets includes Autodesk, Inc., Automatic Data Processing, Inc., Avaya Holdings Corp., Benefitfocus, Inc., Black Knight, Inc., Blackbaud, Inc., BlackBerry Limited, Booz Allen Hamilton Holding Corporation Class A, Bottomline Technologies (de), Inc., Broadridge Financial Solutions, Inc., CACI International Inc Class A, Cadence Design Systems, Inc., Cardtronics plc Class A, Cass Information Systems, Inc., Ceridian HCM Holding, Inc., CGI Inc. Class A, Check Point Software Technologies Ltd., Cheetah Mobile, Inc. ADR Class A, Cision Ltd., Citrix Systems, Inc., Cloudera, Inc., Cognizant Technology Solutions Corporation Class A, CommVault Systems, Inc., Conduent, Inc., CooTek (Cayman) Inc. Sponsored ADR Class A, CoreLogic, Inc., CSG Systems International, Inc., CyberArk Software Ltd., Diamond S Shipping Group, Inc., DXC Technology Co., Ebix, Inc., Endava Plc Sponsored ADR Class A, Endurance International Group Holdings, Inc., Envestnet, Inc., EPAM Systems, Inc., Euronet Worldwide, Inc., Everi Holdings, Inc., EVERTEC, Inc., EVO Payments, Inc. Class A, ExlService Holdings, Inc., Fair Isaac Corporation, Fidelity National Information Services, Inc., FireEye, Inc., Fiserv, Inc., FleetCor Technologies, Inc., ForeScout Technologies, Inc., Formula Systems (1985) Ltd. Sponsored ADR, Fortinet, Inc., Gartner, Inc., GDS Holdings Ltd. Sponsored ADR Class A, Genpact Limited, Global Payments Inc., Globant SA, GoDaddy, Inc. Class A, GreenSky, Inc. Class A, GTT Communications, Inc., Guidewire Software, Inc., HubSpot, Inc., Instructure, Inc., International Business Machines Corporation, Interxion Holding N.V., Intuit Inc., Ituran Location and Control Ltd., Jack Henry & Associates, Inc., Leidos Holdings, Inc., LivePerson, Inc., LiveRamp Holdings, Inc., LogMeIn, Inc., Manhattan Associates, Inc., ManTech International Corporation Class A, Mastercard Incorporated Class A, Materialise NV Sponsored ADR, MAXIMUS, Inc., Microsoft Corporation, MicroStrategy

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For the top 10 holdings of WCLD please visit the Fund's fund detail page at <https://www.wisdomtree.com/etfs/megatrends/wcld>

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For more investing insights, check out our [Economic & Market Outlook](#)

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**U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.**

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You cannot invest directly in an index.

## DEFINITIONS

**Software-as-a-Service (SaaS)** : Software applications provided over a network connectio.

**BVP Nasdaq Emerging Cloud Index** : designed to track the performance of emerging public companies primarily involved in providing cloud software to their customers.