

VALUE FOCUS

FinTech Industry

Mid-Year 2019

Broader markets increased 18% in the first half of 2019 as markets rebounded from the decline in the fourth quarter of 2018. Despite the strong returns in the first half of 2019, investors and markets continued to weigh concerns about enhanced volatility given the potential for slower growth in 2019, political and trade uncertainty, and a variety of other economic factors (nearly inverted Treasury curve, decline in oil prices, and weaker home sales).

Related to FinTech specifically, all three FinTech niches that we track outperformed the S&P 500 in the trailing twelve month period as declines in the fourth quarter of 2018 were offset by strong gains for the sector in the first half of 2019. A large portion of this outperformance occurred in the first half of 2019.

FinTech M&A activity was relatively steady in 2018 and the first half of 2019 (compared to 2017) as measured by number of transactions. However, there was a marked increase in median deal values driven by activity involving larger transactions (a significantly higher number of deals with values exceeding \$500 million and \$1 billion in the year-to-date period). Similarly, FinTech fundraising in the U.S. was strong in the first half of 2019 due to some larger deals. The largest portion of funding was to lending and payments startups.

While interest in the FinTech sector remains high, the outlook remains uncertain as competitive pressures, continuing technological change, and regulatory/policy uncertainty remain.



FinTech Industry Services

Mercer Capital provides financial technology companies with valuation, financial advisory, and consulting services.

Services Provided

- Valuation of financial technology companies
- Financial advisory/valuations for acquisitions and divestitures
- Valuations for purchase accounting and impairment testing
- Fairness and solvency opinions
- Litigation support for economic damages and valuation and shareholder disputes
- Consulting and board presentations for corporate and strategic planning

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BONUS ARTICLE

Key Valuation Considerations for FinTech Purchase Price Allocations

FinTech M&A continues to be top of mind for the sector as larger players seek to grow and expand while founders and early investors look to monetize their investments.

In this article, we discuss one of the most significant assets to be considered in FinTech acquisitions, customer relationships, and how to value these assets.

Learn More about Mercer Capital & our FinTech Services at

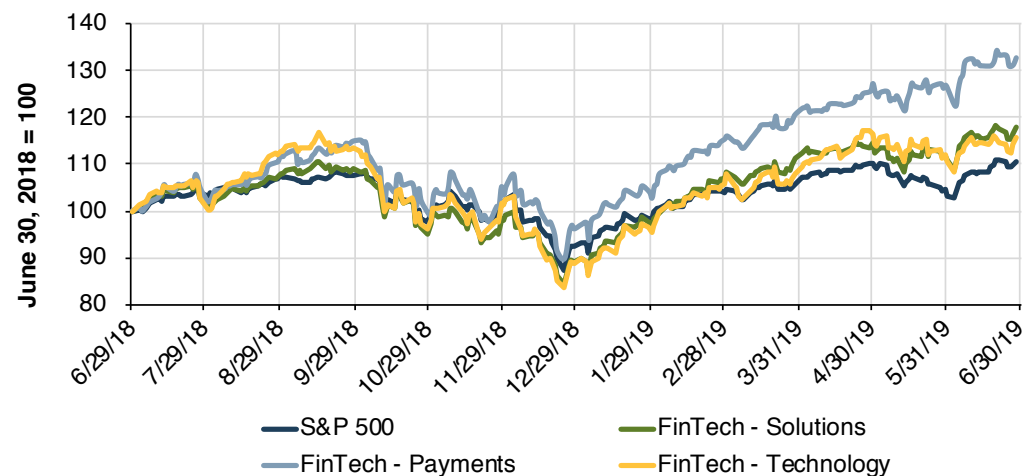
<http://mer.cr/FinTech>

Public Market Indicators

In the last twelve months, all three FinTech niches of Payments, Technology and Solutions outperformed the market despite dropping more than the market in 4Q18.

The Payments, Solutions, and Technology niches returned ~15-32% and outperformed the S&P 500 which was up ~10% in the trailing twelve month period.

FinTech IPO's were relatively slow with only one IPO in the U.S. thus far into 2019 as AssetMark Financial Holdings, Inc. IPO'd in July of 2019. AMK provides wealth management and technology solutions that power independent financial advisers and their clients.



Source: S&P Global Market Intelligence

Valuation Multiples as of June 30, 2019

Segment	"Price/ LTM EPS"	"Price / 2019 (E) EPS"	"Price / 2020 (E) EPS"	"Ent'p Value / LTM EBITDA"	Ent'p Value / FY19 (E) EBITDA	Ent'p Value / FY20 (E) EBITDA	"Ent'p Value / LTM Revenue"
FinTech - Payments	38.5	26.2	22.4	20.3	16.9	14.3	5.2
FinTech - Solutions	47.9	26.3	22.7	20.7	15.4	14.3	4.6
FinTech - Technology	38.9	32.1	27.1	20.5	19.9	14.3	4.5

Source: S&P Global Market Intelligence

FINTECH NEWSLETTER: PUBLIC MARKET INDICATORS

Each quarter, the FinTech newsletter reviews the public FinTech market.

To receive quarterly updates, follow the link below.

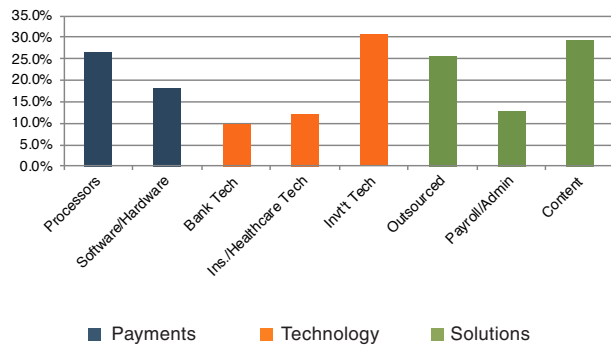
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- Consistent with recent historical growth patterns and outlook near-term, FinTech companies remain priced at a premium to the broader markets with the S&P 500 priced at ~16x estimated forward earnings at mid-year 2019 (per FactSet).
- Investors continue to weigh market potential and growth for the sector against recent FinTech performance and profitability while traditional financial incumbents are weighing whether to enter FinTech partnerships, develop their own in-house solutions or acquire FinTech companies.
- The Technology niche reported the highest P/E and EV/EBITDA multiples compared to the other two niches, primary reflecting their lower margins as price-to-revenue multiples were lower than other niches.

Segment	Month-to-Date	Year-to-Date	Last 12 Months	Price / LTM EPS	Price / 2019 (E) EPS	Price / 2020 (E) EPS	Ent'p Value / LTM EBITDA	Ent'p Value / FY19 (E) EBITDA	Ent'p Value / FY20 (E) EBITDA	Ent'p Value / LTM Revenue
FinTech - Payments	4.6%	11.0%	36.7%	38.5	26.2	22.4	20.3	16.9	14.3	5.2
FinTech - Solutions	5.4%	7.1%	30.9%	47.9	26.3	22.7	20.7	15.4	14.3	4.6
FinTech - Technology	3.0%	8.0%	28.6%	38.9	32.1	27.1	20.5	19.9	14.3	4.5

FinTech Margins

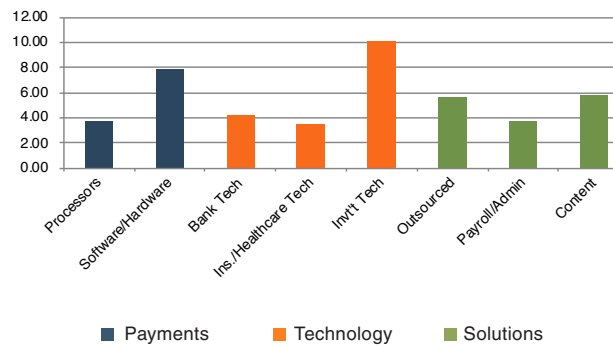
EBITDA Margin (LTM)



Source: S&P Global Market Intelligence

FinTech Revenue Multiples

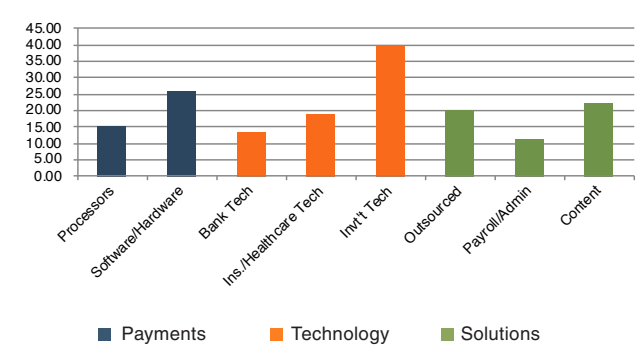
EV / Revenue (LTM)



Source: S&P Global Market Intelligence

FinTech EBITDA Multiples

EV / EBITDA (LTM)



Source: S&P Global Market Intelligence

FinTech M&A

Mid Year 2019

Deal activity as measured by number of transactions was relatively steady in 2018 and the first half of 2019 (compared to 2017).

When examining this by niche, the Payments and Technology niches had a significant increase in activity year-to-date.

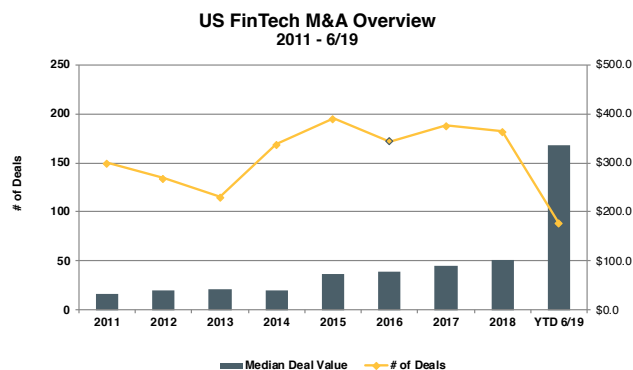
However, there was a marked increase in median deal values driven by activity involving larger transactions (a significantly higher level of deals with values exceeding \$500 million and \$1 billion in the year-to-date period).

Several of the larger transactions were within the Payments and Solutions niches.

Deal value/revenue multiples in 2018 and the first half of 2019 were also up relative to 2017 and 2016 levels as well, reflecting continued market strength, acquirer interest, and a greater proportion of larger transactions.

Globally, FinTech fundraising fell in the first half of 2019 at \$22 billion compared to \$31 billion in the first half of 2018. This primarily reflected a slowdown in China and some larger funding rounds in the first half of 2018.

In the U.S., FinTech fundraising was strong with a 60% increase in the first half of 2019 to ~\$13 billion, reflecting some larger deals. The largest portion of funding was to lending startups (29% of total) and payments (25% of total).



Deal Activity

	YTD 6/19	2018	2017	2016	% Chg. 18/17
# of Deals	89	182	188	194	-3.2%
Total Reported Deal Value (\$M)	\$110,210.8	\$88,052.6	\$17,403.7	\$20,716.3	405.9%
Median Reported Deal Value (\$M)	\$335.0	\$100.9	\$89.5	\$39.6	12.7%

Deal Activity by FinTech Industry Niche

	YTD 6/19	2018	2017	2016	% Chg. 18/17
Payments Total	30	39	44	35	-11.4%
Technology Total	40	92	104	106	-11.5%
Solutions Total	19	51	40	53	27.5%

Median Pricing Metrics

	YTD 6/19	2018	2017	2016	% Chg. 18/17
Deal Value / Revenue	5.82x	3.75x	3.13x	2.32x	19.8%
Deal Value Greater than \$1BN	8	15	4	1	275.0%
Deal Value Greater than \$500M	12	17	9	4	88.9%
Deal Value Greater than \$50M	25	43	38	24	13.2%

Median Deal Value (\$M)

	6/19	2018	2017	2016
Payments	\$500.0	\$126.0	\$213.5	\$258.0
Technology	\$121.0	\$68.3	\$59.6	\$25.0
Solutions	\$68.1	\$142.3	\$119.0	\$37.0

Publicly Traded Payments Companies

Ticker	Name	6/3/19 Price	Market Cap (\$M)	Ent'p Val (\$M)	Price / Earnings			Ent'p Value / EBITDA			EV / LTM	LTM Total		LTM Margins	
					LTM	FY19E	FY20E	LTM	FY19E	FY20E	Revenue	Revenue (\$M)	EBITDA (\$M)	EBITDA	Net Inc.
Payment Processors															
ADS	Alliance Data Systems Corporation	140.13	7,341	28,720	7.9	7.3	5.9	15.2	18.8	17.2	3.6	7,695	1,780	23%	11%
CATM	Cardtronics plc	27.32	1,265	2,102	119.5	13.1	12.0	7.9	7.2	6.8	1.6	1,327	269	20%	1%
PMTS	CPI Card Group Inc.	2.50	28	330	NM	NM	NM	12.6	8.6	8.0	1.3	273	29	11%	-5%
DLX	Deluxe Corporation	40.66	1,774	2,704	14.8	6.9	6.8	6.0	5.8	5.9	1.4	2,011	428	21%	5%
EEFT	Euronet Worldwide, Inc.	168.24	8,742	8,677	38.5	24.1	20.6	17.9	14.0	12.1	3.4	2,633	511	19%	10%
EVRI	Everi Holdings Inc.	11.93	848	1,880	62.6	46.5	30.3	8.4	7.4	6.8	3.9	493	230	47%	4%
EVTC	EVERTEC, Inc.	32.70	2,304	2,824	27.0	17.1	15.8	15.8	12.8	12.1	6.1	472	186	39%	21%
FDC	Filinvest Development Corporation	0.27	2,363	4,791	11.2	-	-	9.4	-	-	3.1	1,497	481	32%	14%
FLT	FleetCor Technologies, Inc.	280.85	24,207	27,734	31.7	24.0	20.8	20.3	18.2	16.1	11.2	2,532	1,417	56%	35%
GPN	Global Payments Inc.	160.13	25,091	30,438	53.7	26.5	22.7	21.8	18.4	16.7	8.8	3,556	1,439	40%	14%
GDOT	Green Dot Corporation	48.90	2,599	1,521	23.7	17.0	12.6	5.4	3.6	2.8	0.9	1,076	186	17%	11%
MA	Mastercard Incorporated	264.53	270,196	272,021	44.2	34.7	29.4	29.5	26.5	22.9	17.7	15,707	9,364	60%	43%
MGI	MoneyGram International, Inc.	2.47	139	898	NM	12.1	8.1	4.7	4.4	4.2	0.7	1,332	157	12%	-6%
SQ	Square, Inc.	72.53	30,678	30,544	NM	95.4	64.0	NM	73.4	47.1	8.5	3,948	34	1%	-1%
TSS	Total System Services, Inc.	128.27	22,700	26,507	39.3	26.3	23.1	22.1	18.1	16.8	6.5	4,103	1,168	28%	15%
V	Visa Inc.	173.55	379,274	390,253	35.9	31.2	26.8	26.7	23.6	20.9	18.0	22,274	15,044	68%	53%
WU	The Western Union Company	19.89	8,567	10,694	11.0	11.2	10.4	8.4	8.9	8.5	2.1	5,467	1,342	25%	22%
WEX	WEX Inc.	208.10	9,000	11,383	68.7	22.3	19.3	22.1	16.0	14.1	7.8	1,591	537	34%	7%
Median			7,954	9,686	35.9	22.3	19.3	15.2	13.4	12.1	3.8	2,271	496	27%	11%

Publicly Traded Payments Companies

Ticker	Name	6/30/19 Price	Market Cap (\$M)	Ent'p Val (\$M)	Price / Earnings			Ent'p Value / EBITDA			EV / LTM	LTM Total		LTM Margins	
					LTM	FY19E	FY20E	LTM	FY19E	FY20E	Revenue	Revenue (\$M)	EBITDA (\$M)	EBITDA	Net Inc.
Payment Software/Hardware															
ADP	Automatic Data Processing, Inc.	165.33	71,956	72,261	42.8	29.0	25.4	21.8	20.2	17.9	5.2	14,175	3,489	25%	16%
EVOP	EVO Payments, Inc.	31.53	1,018	2,050	NM	55.2	43.9	29.8	11.5	10.2	3.4	530	117	22%	-7%
IIIV	i3 Verticals, Inc.	29.45	424	621	93.2	35.1	28.3	21.2	14.1	11.5	1.7	352	25	7%	0%
NSP	Insperty, Inc.	122.14	5,039	4,891	31.6	26.0	22.2	22.0	16.9	14.3	1.2	4,088	225	5%	4%
PYPL	PayPal Holdings, Inc.	114.46	134,483	129,074	61.9	38.3	32.5	45.9	27.3	22.7	8.1	16,342	2,989	18%	15%
PAYX	Paychex, Inc.	82.29	29,567	29,651	28.8	28.4	25.5	19.1	18.2	16.8	7.9	3,773	1,558	41%	27%
WDAY	Workday, Inc.	205.58	46,542	46,179	NM	121.7	92.0	NM	65.9	49.2	15.2	3,029	(270)	-9%	-15%
PAYC	Paycom Software, Inc.	226.72	13,039	13,005	92.7	69.0	54.9	63.3	43.7	35.0	21.2	653	219	34%	24%
PCTY	Paylocity Holding Corporation	93.82	4,970	4,808	123.1	64.1	51.3	80.5	32.9	26.7	10.9	468	74	16%	12%
TNET	TriNet Group, Inc.	67.80	4,745	4,924	24.3	20.0	17.8	16.8	12.8	11.4	1.4	3,661	266	7%	5%
UPLD	Upland Software, Inc.	45.53	1,151	1,355	NM	21.6	20.6	35.3	18.3	16.6	8.5	184	44	24%	-9%
Median			5,039	4,924	52.3	35.1	28.3	25.9	18.3	16.8	7.9	3,029	219	18%	5%
Overall Payments Median			7,341	8,677	38.5	26.2	22.4	20.3	16.9	14.3	5.2	2,532	269	23%	11%

Publicly Traded Solutions Companies

Ticker	Name	6/30/19 Price	Market Cap (\$M)	Ent'p Val (\$M)	Price / Earnings			Ent'p Value / EBITDA			EV / LTM	LTM Total		LTM Margins	
					LTM	FY19E	FY20E	LTM	FY19E	FY20E	Revenue	Revenue (\$M)	EBITDA (\$M)	EBITDA	Net Inc.
Outsourced															
CSGS	CSG Systems International, Inc.	48.83	1,559	1,886	22.4	15.1	14.1	12.2	8.8	8.6	2.0	951	159	17%	8%
EFX	Equifax Inc.	135.24	16,340	19,261	NM	24.0	22.0	28.0	16.1	14.8	5.6	3,396	673	20%	-13%
EXLS	ExlService Holdings, Inc.	66.13	2,271	2,375	48.0	22.6	20.3	19.4	14.4	12.8	2.6	949	128	14%	5%
FICO	Fair Isaac Corporation	314.02	9,103	9,847	63.4	41.5	36.0	39.5	27.8	24.4	9.1	1,144	292	25%	16%
FIS	Fidelity National Information Services, Inc.	122.68	39,703	48,622	49.8	16.5	15.3	20.4	14.8	13.8	5.8	8,420	2,446	29%	9%
FISV	Fiserv, Inc.	91.16	35,775	41,491	37.6	26.4	23.7	21.8	17.7	16.7	7.1	5,977	1,929	32%	16%
INTU	Intuit Inc.	261.33	67,748	64,850	47.7	38.2	32.8	33.2	25.8	22.9	9.8	6,593	1,952	30%	22%
PRGX	PRGX Global, Inc.	6.72	158	191	126.8	48.0	29.2	13.5	6.6	5.8	1.1	174	12	7%	1%
SSNC	SS&C Technologies Holdings, Inc.	57.61	14,575	22,685	111.5	15.1	13.6	16.9	12.2	11.3	5.5	4,389	1,591	36%	7%
Median			14,575	19,261	48.9	24.0	22.0	20.4	14.8	13.8	5.6	3,396	673	25%	8%

Publicly Traded Solutions Companies

Ticker	Name	6/30/19 Price	Market Cap (\$M)	Ent'p Val (\$M)	Price / Earnings			Ent'p Value / EBITDA			EV / LTM	LTM Total		LTM Margins	
					LTM	FY19E	FY20E	LTM	FY19E	FY20E	Revenue	Revenue (\$M)	EBITDA (\$M)	EBITDA	Net Inc.
Payroll/Administration															
ACIW	ACI Worldwide, Inc.	34.34	3,797	5,131	63.9	27.0	21.3	26.8	11.9	10.2	4.3	1,069	174	16%	8%
EPAY	Bottomline Technologies (de), Inc.	44.24	1,926	1,937	105.9	33.0	29.9	43.5	19.4	18.0	4.6	422	47	11%	2%
BR	Broadridge Financial Solutions, Inc.	127.68	14,829	16,025	30.1	26.2	24.0	17.0	16.1	15.4	3.5	4,362	913	21%	11%
CDK	CDK Global, Inc.	49.44	6,014	8,647	16.8	13.0	11.3	11.5	10.2	10.1	3.7	1,915	698	36%	6%
DBD	Diebold Nixdorf, Incorporated	9.16	702	2,864	NM	NM	9.6	11.0	7.3	6.6	0.6	4,587	350	8%	-12%
NCR	NCR Corporation	31.10	3,736	7,918	NM	11.1	9.8	9.7	7.6	7.2	1.2	6,597	835	13%	2%
NTWK	NetSol Technologies, Inc.	5.59	65	68	10.3	11.4	11.6	6.1	-	4.4	1.0	67	12	17%	9%
PEGA	Pegasystems Inc.	71.21	5,619	5,533	NM	NM	145.3	NM	130.7	78.0	6.3	878	(50)	-6%	-6%
WK	Workiva Inc.	58.09	2,623	2,526	NM	NM	NM	NM	NM	NM	10.0	269	(21)	-8%	-13%
Median			3,736	5,131	30.1	19.6	16.5	11.5	11.0	10.1	3.7	1,069	174	13%	2%
Content															
CLGX	CoreLogic, Inc.	41.83	3,375	5,193	35.7	16.8	14.8	13.8	11.0	10.3	2.9	1,732	342	20%	2%
CSGP	CoStar Group, Inc.	554.06	20,246	19,092	74.6	55.1	46.5	48.4	38.4	32.2	15.4	1,293	426	33%	22%
DNB	DNB ASA	18.61	29,564	113,054	9.9	10.4	10.1	-	-	-	-	6,319	NA	na	49%
FDS	FactSet Research Systems Inc.	286.56	10,958	11,182	33.7	28.6	26.5	22.6	21.4	19.9	7.9	1,417	496	35%	23%
TRU	TransUnion	73.51	13,766	17,671	50.3	27.7	24.3	20.7	17.3	15.8	7.4	2,498	890	36%	13%
FORR	Forrester Research, Inc.	47.03	867	1,019	226.2	29.2	23.4	32.4	22.2	15.0	2.7	412	32	8%	-1%
IT	Gartner, Inc.	160.94	14,499	17,367	90.7	40.7	35.3	29.4	23.9	21.3	4.4	4,052	591	15%	5%
MORN	Morningstar, Inc.	144.64	6,170	5,910	35.8	-	-	22.1	-	-	5.8	1,057	272	26%	17%
VRSK	Verisk Analytics, Inc.	146.46	23,970	26,605	40.9	33.2	29.9	24.9	21.8	20.2	10.9	2,490	1,092	44%	24%
Median			13,766	17,367	40.9	28.6	24.3	22.6	21.4	15.8	5.8	1,732	461	29%	17%
Overall Solutions Median			6,170	8,647	47.9	26.3	22.7	20.7	15.4	14.3	4.6	1,732	388	20%	8%

Publicly Traded Technology Companies

Ticker	Name	6/30/19 Price	Market Cap (\$M)	Ent'p Val (\$M)	Price / Earnings			Ent'p Value / EBITDA			EV / LTM	LTM Total		LTM Margins	
					LTM	FY19E	FY20E	LTM	FY19E	FY20E	Revenue	Revenue (\$M)	EBITDA (\$M)	EBITDA	Net Inc.
Banking Technology															
GSKY	Jack Henry & Associates, Inc.	133.92	10,339	10,339	35.8	37.9	33.6	21.6	19.9	18.5	6.4	1,603	478	30%	18%
QTWO	Q2 Holdings, Inc.	76.36	3,567	3,396	NM	NM	165.7	NM	174.3	87.9	14.1	277	(29)	-11%	-21%
JKHY	GreenSky, Inc.	12.29	745	829	98.0	17.0	13.5	5.4	3.8	3.1	1.8	466	146	31%	7%
PFMT	Performant Financial Corporation	1.05	56	115	NM	NM	NM	NM	NM	8.3	0.8	138	(16)	-12%	-20%
Median			2,156	2,113	66.9	27.4	33.6	13.5	19.9	13.4	4.1	371	65	10%	-6%
Insurance/Healthcare Technology															
CRVL	CorVel Corporation	87.01	1,610	1,608	35.4	-	-	18.0	-	-	2.5	595	90	15%	8%
CRDB	Crawford & Company	9.31	502	792	21.9	11.7	10.5	9.5	6.7	6.3	0.8	1,023	89	9%	3%
EBIX	Ebix, Inc.	50.22	1,533	2,279	17.0	11.5	9.4	13.4	10.6	10.1	4.3	552	171	31%	17%
GWRE	Guidewire Software, Inc.	101.38	8,294	7,595	143.7	80.4	69.8	106.6	47.5	36.2	10.1	752	71	9%	8%
HMSY	HMS Holdings Corp.	32.39	2,821	2,817	41.0	27.5	25.1	20.9	16.3	14.5	4.7	626	154	25%	16%
MGLN	Magellan Health, Inc.	74.23	1,785	2,403	138.4	30.7	21.6	17.6	9.2	7.8	0.3	7,226	136	2%	0%
CSLT	Castlight Health, Inc.	3.23	465	423	NM	287.1	48.8	NM	55.1	25.5	2.7	154	(27)	-17%	-20%
HQY	HealthEquity, Inc.	65.40	4,102	3,813	44.7	49.2	41.1	36.9	27.0	22.5	12.5	304	103	34%	31%
INOV	Inovalon Holdings, Inc.	14.51	2,224	3,147	NM	32.1	27.1	20.2	15.3	13.8	5.4	585	161	27%	-3%
EVH	Evolent Health, Inc.	7.95	652	872	NM	NM	54.6	NM	203.7	14.1	1.2	733	(48)	-7%	-15%
Median			1,697	2,341	41.0	30.7	26.1	19.1	15.8	13.9	3.5	611	97	12%	5%
Investment Technology															
ENV	Envestnet, Inc.	68.37	3,546	4,172	NM	32.1	25.7	50.0	19.9	16.0	4.7	837	81	10%	-2%
MSCI	MSCI Inc.	238.79	20,220	22,214	36.8	38.1	33.3	29.5	26.4	23.7	15.4	1,477	767	52%	39%
Median			11,883	13,193	36.8	35.1	29.5	39.7	23.1	19.9	10.0	1,157	424	31%	19%
Overall Technology Median			2,004	2,610	38.9	32.1	27.1	20.5	19.9	14.3	4.5	611	97	12%	5%



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Bonus Article

Key Valuation Considerations for FinTech Purchase Price Allocations

FinTech M&A continues to be top of mind for the sector as larger players seek to grow and expand while founders and early investors look to monetize their investments. This theme was evident in several larger deals already announced in 2019 including Global Payments/Total System Services (TSYS), Fidelity National Information Services, Inc./Worldpay, Inc., and Fiserv, Inc./First Data Corporation.

One important aspect of FinTech M&A is the purchase price allocation and the valuation estimates for goodwill and intangible assets as many FinTech companies have minimal physical assets and a high proportion of the purchase price is accounted for via goodwill and intangible assets. The majority of value creation for the acquirer and their shareholders will come from their investment in and future utilization of the intangibles of the FinTech target. To illustrate this point, consider that the median amount of goodwill and intangible assets was ~98% of the transaction price for FinTech transactions announced in 2018. Since such a large proportion of the transaction price paid for FinTech companies typically gets carried in the form of goodwill or intangibles on the acquirer's balance sheet, the acquirer's future earnings, tax expenses, and capitalization will often be impacted significantly from the depreciation and amortization expenses.

When preparing valuation estimates for a purchase price allocation for a FinTech company, one key step for acquirers is identifying the intangible assets that will need to be valued. In our experience, the identifiable intangible assets for FinTech acquisitions often include the tradename, technology (both developed and in-development), non-compete agreements, and customer relationships. Additionally, there may be a need to

consider the value of an earn-out arrangement if a portion of transaction consideration is contingent on future performance as this may need to be recorded as a contingent liability.

Since the customer relationship intangible is often one of the more significant intangible assets to be recorded in FinTech acquisitions (both in \$ amounts and as a % of the purchase price), we discuss how to value FinTech customer relationships in greater detail in the remainder of the article.

Valuing Customer-Related Assets

Firms devote significant human and financial resources in developing, maintaining and upgrading customer relationships. In some instances, customer contracts give rise to identifiable intangible assets. More broadly, however, customer-related intangible assets consist of the information gleaned from repeat transactions, with or without underlying contracts. Firms can and do lease, sell, buy or otherwise trade such information, which are generally organized as customer lists.

Since FinTech has some relatively varied niches including payments, digital lending, WealthTech, or InsurTech, the valuation of FinTech customer relationships can vary depending on the type of company and the niche that it operates in. While we do not delve into the key attributes to consider for each FinTech niche, we provide one illustration from the Payments niche.

In the Payments industry, one key aspect to understand when evaluating customer relationships is where the company is in the payment loop and whether the company operates in a B2B (business-to-business) or B2C (business-to-consumer) model. This will drive who the customer is and the economics related to valuing the cash flows from the customer relationships. For example, merchant acquirers typically have contracts with the merchants themselves and the valuable customer relationship lies with the merchant and the dollar volume of transactions processed by the merchant over time, whereas the valuable relationship with other payments companies such as a prepaid or gift card company may lie with the end-user or consumer and their spending/card usage habits over time.

Valuation Approaches

Valuation involves three approaches: 1) the cost approach, 2) the market approach, and 3) the income approach. Customer relationships are typically valued based upon an income approach (i.e., a discounted cash flow method) where the cash flows that the customer relationships are expected to generate in the future are forecast and then discounted to the present at a market rate of return.

Cost Approach

Valuation under the cost approach requires estimation of the cost to replace the subject asset, as well as opportunity costs in the form of cash flows foregone as the replacement is sought or recreated. The cost approach may not be feasible when replacement or recreation periods are long. Therefore, the cost approach is used infrequently in valuing customer-related assets.

Market Approach

Use of the market approach in valuing customer-related assets is generally untenable for FinTech companies because transactional data on sufficiently comparable assets are not likely to be available.

Income Approach

Under the income approach, customer-related assets are valued most commonly using the income approach. One method within the income approach that is often used to value FinTech customer relationships is the Multi-Period Excess Earnings Method (MPEEM). MPEEM involves the estimation of the cash flow stream attributable to a particular asset. The cash flow stream is discounted to the present to obtain an indication of fair value. The most common starting point in estimating future cash flows is the prospective financial information prepared by (or in close consultation with) the management of the subject business. The key valuation inputs are often estimates of the economic benefit of the customer relationship (i.e., the cash flow stream attributable to the relationships), customer attrition rate, and the discount rate. Three key attributes that are important when using these inputs to valuing customer relationships include:

- 1. Repeat Patronage.** The expectation of repeat patronage creates value for customer-related intangible assets. Contractual customer relationships formally codify the expectation of future transactions. Even in the absence of contracts, firms look to build on past interactions with customers to sell products and services in the future.

Two aspects of repeat patronage are important in evaluating customer relationships. First, not all customer contact leads to an expectation of repeat patronage. The quality of interaction with walk-up retail customers, for instance, is generally considered inadequate to reliably lead to expectations of recurring business. Second, even in the presence of adequate information, not all expected repeat business may be attributable to customer-related intangible assets. Some firms operate in monopolistic or near-monopolistic industries where repeat patronage is directly attributable to a dearth of acceptable alternatives available to customers. In other cases, it may be more appropriate to attribute recurring business to the strength of the trade names, software platform, or brands.

- 2. Attrition.** Customer-related intangible assets create value over a finite period. Without efforts geared towards continual reinforcement, customer lists dwindle over time due to customer mortality, the ravages of competition, or the emergence of alternate products and services. The mechanics of present value mathematics further erode the economic benefits of sales to current customers in the distant future. Customer relationships are wasting assets whose economic value attrite with the passage of time.
- 3. Other Assets.** Customer-related intangible assets depend on the existence of other assets to provide value to the firm. Most assets, including fixed assets and intellectual property, are essential in creating products or providing services. The act of selling these products and services enable firms to develop relationships and collect information from customers. In turn, the value of these relationships depends on the firms' ability to sell additional products and services in the future. Consequently, for firms to extract value from customer related assets, a number of other assets need to be in place.

Conclusion

Mercer Capital has experience providing valuation and advisory services to FinTech companies and their acquirers. We have valued customer-related and other intangible assets to the satisfaction of clients and their auditors within the FinTech industry across a multitude of niches (payments, wealth management, insurance, lending, and software). Most recently, we completed a purchase price allocation for a private equity firm that acquired a FinTech company in the Payments niche. Please contact us to explore how we can help you.



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