EQUITY RESEARCH

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DYE & DURHAM LTD.

Acquiring U.K.-based Insight Legal Software

Outperformer

DND-TSX, Sector: Information Technology

Current Price (1/23/23):	C$21.08
Price Target (12-18 mos.):	C$27.50

Our Conclusion

Dye & Durham announced the acquisition of Insight Legal Software, a U.K.-based provider of legal practice management software. Terms of the acquisition were not announced, although we expect the business is generating revenue in the mid-single-digit millions. While the deal itself will not make a material contribution to DND's 2023 revenue, the acquisition (and CEO Matt Proud's comments on the deal) appears to signal a focus on smaller tuck-in acquisitions after the year-long pursuit of Link Group ended unsuccessfully. With **leverage at the business remaining elevated** and floating rate debt putting pressure on free cash flow as housing sales likely remain depressed into 2023, we take a positive view on DND's focus on smaller acquisitions.

Key Points

Insight Expands U.K. Presence: Insight Legal Software provides legal practice management software designed specifically for U.K. and Ireland law firms. Services include finance/accounting, case management, practice management, compliance, billing, and time recording. The press release announcing the deal noted that Insight has 900 clients and 5,000 users. With information on Insight's website indicating a monthly user fee of ~£70, we believe that recurring revenue is ~£4MM, with potential for additional professional services revenue. Applying DND's own margin profile (~55%) to Insight and its typical 10x EBITDA acquisition multiple results in a purchase price in the range of $30MM-$40MM at current exchange rates.

Smaller Deals Likely To Be The Focus: In an interview discussing the deal, CEO Matt Proud noted that given the current macroeconomic environment DND is more focused on smaller tuck-in deals rather than transformational ones. In the same interview Mr. Proud also noted that DND did not intend to increase prices on Insight's services and would focus on cross-selling its solutions into Insight's customer base. Commentary on the size of M&A targets and the focus on cross-selling rather than price increases appear to signal a change in DND's approach to M&A in response to the macroeconomic environment and regulatory activity.

Unlikely To Attract CMA Scrutiny: The legal practice management service market is less concentrated than the U.K. property search market, in our view making it less likely to attract the level of regulatory scrutiny that challenged the TM Group acquisition. In August 2022, the U.K. Competition and Markets Authority (CMA) required that Dye & Durham divest TM Group, and DND remains in the process of trying to find a buyer. In the CMA's decision, it noted that the acquisition of TM Group would create the largest player in the market and leave only two other national providers of property search services, a level of concentration that DND and Insight would not hold in the legal practice management market.

All figures in Canadian dollars unless otherwise stated.

Please see "Price Target Calculation and Key Risks to Price Target" information on page 2.
For required regulatory disclosures please refer to "Important Disclosures" beginning on page 3.

Price Target Calculation

We derive our price target of $27.50 by applying a 10x EV/EBITDA multiple to our F2024 EBITDA estimate based on the current capital structure and sale of TM Group. The 10x multiple is a 1x discount to the peak trading multiple of comparable registry services providers. We also include $5/share of value for the value of future M&A. That value is calculated using a discounted cash flow (DCF) that assumes 75% of free cash flow (FCF) reinvested in M&A, an average acquisition multiple of 6.5x sales and a 10% discount rate.

Key Risks To Price Target

The primary risks to our price target include the following: 1) competition and regulatory reviews impact the ability to acquire; 2) regulatory reviews and negative media coverage limit the ability to increase prices on e-conveyancing and transactional services; 3) slowdowns in housing market sales impact transactional revenues, putting organic growth at risk; 4) risks related to the integration of M&A given the pace of acquisition; and, 5) governance concerns in the wake of the stock option grant post the take-private process.

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CIBC World Markets Inc. Price Chart

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