

EQUITY RESEARCH

July 17, 2023

Flash Research

CONSTELLATION SOFTWARE INC.

Acquiring Black Knight's Optimal Blue For \$700 Million

Our Conclusion

Constellation announced that its Perseus operating group has entered a binding commitment with Intercontinental Exchange Inc. (ICE) and Black Knight to acquire Black Knight's Optimal Blue business for \$700MM. We estimate Optimal Blue contributed ~\$120MM in revenue to Black Knight in 2022, resulting in a 5x-6x revenue multiple paid by Constellation. The proposed acquisition follows Constellation's acquisition of Black Knight's Empower loan origination system (LOS) business in March as ICE/Black Knight seek FTC approval of its merger. With the FTC still seeking action against the merger, we see Constellation as opportunistically acquiring Optimal Blue, as evidenced by the steep discount in valuation when compared to Black Knight's original purchase price of \$1.8B for the same assets in 2020. The deal is contingent on the close of the ICE/Black Knight transaction.

Key Highlights

About Optimal Blue: Optimal Blue is a provider of secondary market solutions and data services, used to facilitate business between mortgage originators and investors. Originators use the platform to access pricing, conduct loan auctions and gain new relationships - and investors use it to monitor and approve originators, distribute pricing in real time and buy loans. Black Knight acquired Optimal Blue in 2020 for \$1.8B and based on disclosure filed at the time, we estimate Optimal Blue added ~\$25MM in quarterly revenue.

ICE's Acquisition Of Black Knight Facing FTC Action: The FTC took action earlier this year to block ICE's proposed acquisition of Black Knight. Intercontinental owns the dominant LOS in the U.S. (Encompass), with Black Knight owning the second largest (Empower). The FTC alleged that the deal would allow Intercontinental to raise costs to lenders, which would then be passed to homebuyers. The FTC also stated that the deal would harm competition for product pricing and eligibility engines (PPEs) and other ancillary services that are add-ons to LOS. Black Knight proposed to remedy the competitive harm by selling its Empower LOS to Constellation. This was announced in March, however the FTC advised that the proposal did not adequately address the anti-competitive effects.

Transaction Details: Constellation will acquire Optimal Blue for \$700MM, structured with a payment from Constellation of \$200MM in cash and the remainder financed by a \$500MM promissory note issued by Constellation to Black Knight, as a subsidiary of ICE, at the closing of the transaction. Completion of the transaction is subject to InterContinental's acquisition of Black Knight as well as the closing of Constellation's acquisition of Black Knight's Empower LOS business entered into in March.

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Outperformer

CSU-TSX, Sector: Information Technology

Current Price (7/17/23): C\$2,754.64

Price Target (12-18 mos.): C\$3,000.00

All figures in US dollars unless otherwise stated (C\$1.317:US\$1.00).

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

Our C\$3,000 price target is based on a sum-of-the-parts methodology. We value CSU (ex-TOI and LMN) at 26x forward EBITDA multiple and CSU's 30% ownership of TOI and 61% ownership of LMN at market values.

Key Risks To Price Target

The primary risks to our price target include the following: 1) ability to scale; 2) ability to acquire; 3) vertical market exposure; 4) lack of detailed disclosure

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None	NA	Sector rating is not applicable.

Note: Broader market averages refer to S&P 500 in the U.S. and S&P/TSX Composite in Canada.

CIBC World Markets Inc. Price Chart

For price and performance charts, please visit CIBC on the web at <https://researchcentral.cibccm.com/#/disclaimer-central-new> or write to CIBC World Markets Inc., 161 Bay Street, 4th Floor, Toronto, ON M5H 2S8, Attn: Research Disclosure Chart Request.

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