

PART 1

Managed Service Providers

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M&A OPPORTUNITIES FOR MANAGED SERVICE PROVIDERS

Small and medium-sized businesses (SMBs) have historically relied on in-house IT support, but there is an emerging trend of these companies outsourcing their IT functions to Managed Service Providers, or MSPs. The MSP sector is large, highly profitable and growing rapidly, with the market expected to reach more than \$300 billion in five years.

However, the market is highly fragmented, with more than 20,000 companies in North America offering a wide variety of IT services, from specialized products to all-in-one solutions. Many MSPs cite growing revenue and marketing and sales as their key challenges to overcome.

As a result, mergers and acquisitions represent an important way for these companies to expand, whether geographically, within their industry segment or menu of services.

In the first part of this series, we describe what MSPs offer and the market opportunity for M&A within the industry. Subsequent articles will discuss how MSPs can benefit from M&A strategies and the role of private equity.

WHAT MSPS HAVE TO OFFER

MSPs can deliver a variety of IT services and support functions for a fixed monthly fee that is usually a lot lower than what companies would have to spend on their own in terms of salaries, benefits, training and workspace.



The benefits of retaining an MSP reach far beyond reducing IT costs, including:

- Time efficiencies
- Industry expertise
- Execution by specialists
- On-call support
- Access to the latest technologies
- Training for in-house employees

In addition to offering these benefits, a managed services partnership can serve as a strategic relationship to take advantage of emerging and innovative technology and continuously transform

and automate the company's operations within a stable cost structure.

There is a large range of services that MSPs offer; the most common ones tend to be related to software production support and maintenance and systems management. MSPs also assist with increasing project capacity, maintaining security compliance, and improving reliability and efficiency of the firm's IT systems.

THE M&A OPPORTUNITY

MSPs are poised to grow rapidly as SMBs learn more about the advantages of utilizing an MSP to outsource their IT functions. Going forward, the global managed services market is expected to continue expanding at a compound annual growth rate of 8.1%, reaching \$329.1 billion in 2025 from its current estimated size of \$223.0 billion.

MSPs tend to be stable. According to a 2019 survey by Datto, nearly half of surveyed MSPs have been operating for 16+ years and 49% of them earn above \$1 million in annual revenue. They're also highly profitable; according to a survey conducted by Solar Winds MSP, companies average 31.6% gross profit margins.

However, according to that same survey, MSPs struggle with growing revenue and with their marketing and sales efforts.

There are currently about 20,000 profitable MSPs in North America that serve SMBs. Not surprisingly, due to the sheer number of MSPs and the variety of services they offer, the industry is extremely fragmented, with companies specializing in just a few offerings. As a result, implementing an M&A growth strategy is an efficient way for MSPs to increase revenue and market share within a geographic region or industry.

NEXT

Strategic M&A Initiatives & Trends for MSPs

THE MSP MARKET CAN BE SPLIT INTO FIVE BROAD CATEGORIES:

MSSPs

Managed Security Service Providers (MSSPs) focus on providing expertise related to security processes. These can range from offering a complete outsourcing of the firm's security programs to specialization in specific areas, such as threat monitoring and regulatory compliance. The most common security offerings tend to be antivirus, advanced firewall and remote monitoring and management solutions.

MASPs

Managed Application Service Providers (MASPs) provide the infrastructure and ongoing support for a cloud solution, including hosting client applications in their own cloud.

MDSPs

Managed Data Service Providers (MDSPs) design and implement databases and systems that can collect information as well as provide security, storage and data backup.

MISPs

Managed Infrastructure Service Providers (MISPs) can offer a single server with one set function or virtualization and private cloud services that allow multiple users within an organization to control their own network resources.

MNSPs

Managed Network Service Providers (MNSPs) cover a large array of capabilities. MNSPs can offer data and voice-management services as well as support for bandwidth upgrades and equipment management. Some companies offer bundled packages that include firewall, policy management, cloud integration and mobile VPN.