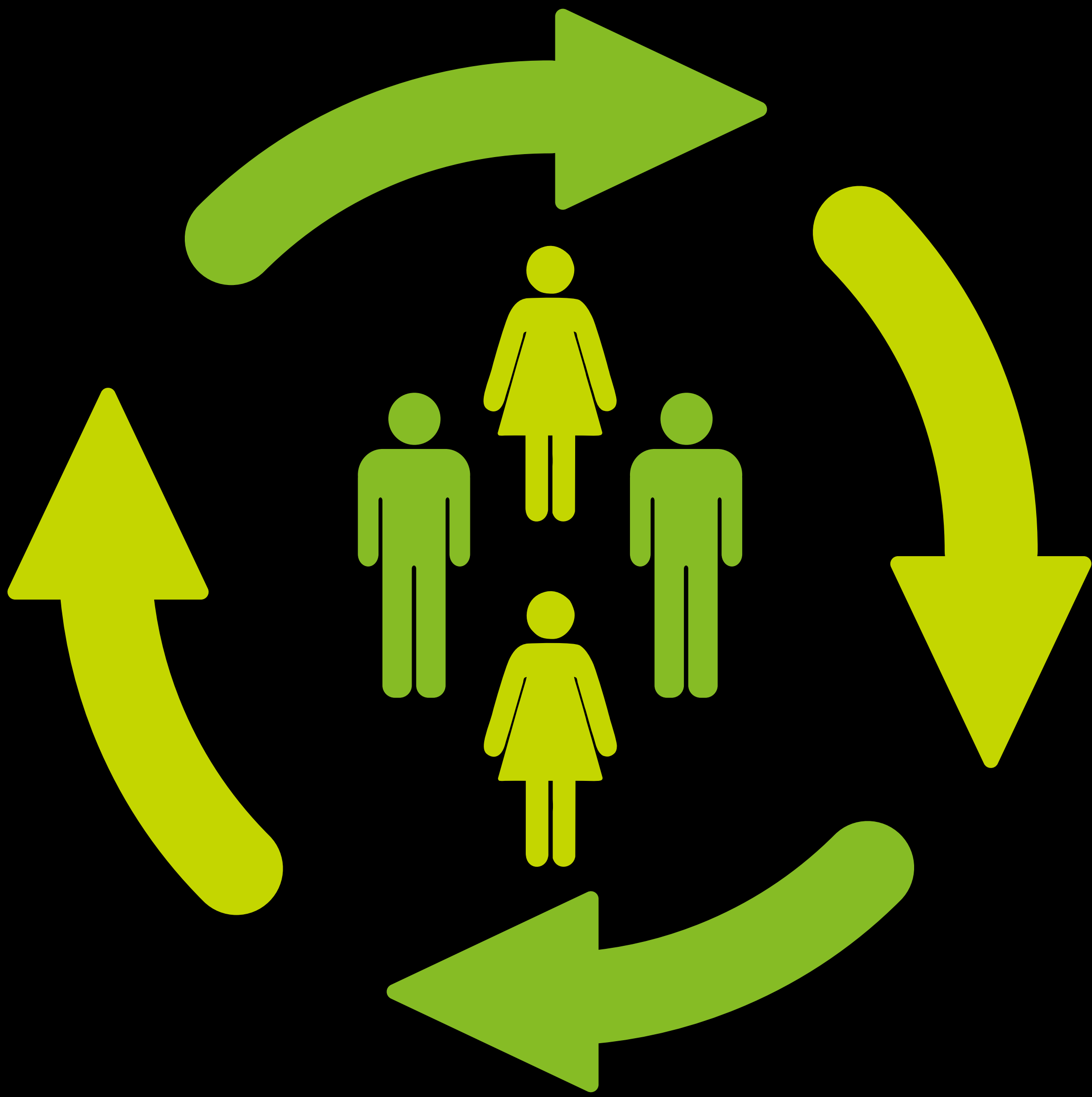
Road to Next



Deloitte.

Data provided by PitchBook

Executive summary

Themes & key findings for this issue:

Per the latest Deloitte Global Human Capital Trends survey, "more than 90 percent of surveyed business leaders believe that using…technology to improve work outcomes and team performance is very important or important to their organization's success. Yet only 22 percent believe their organizations are very ready to use technology to improve work outcomes and team performance."[1]

- **As a result, dealmaking in work software companies has remained resilient even amid volatility, with nearly 1,100 completed transactions for well over $30 billion in aggregate in 2022.**
- **Overwhelmingly, the most recent edition of the Deloitte Global Human Capital Trends survey spanning future workforce tech, preferences, and more signals evolution in employees' desires for more flexible, skills-based work and consequent organizational structures.[2]**
- **Looking forward, ongoing market volatility is prompting slowdowns in dealmaking, which is providing sufficient motive and opportunity for organizations to retool and reinvest in innovative work software to help rethink organizational structures, talent development, and more.**

Heather Gates
Audit & Assurance Private Growth Leader
Deloitte & Touche LLP

With more than 30 years of financial services experience, Heather serves as the national Private Growth Leader, with oversight of the Deloitte Private, Emerging Growth Company, and Private Equity businesses within Audit & Assurance.

Amy Hubler
Audit & Assurance Managing Director,
Future of Work
Deloitte & Touche LLP

With close to 25 years of audit and assurance experience and in leading the Future of Work team, Amy focuses on transforming the Audit & Assurance business' work, workforce, and workplace.

"As part of the future of work, better adapting to evolving talent needs is critical. Capturing professionals' preferences and development opportunities can allow use of analytics to match professionals to optimal career experiences. How can we help our people find the best assignments for their skillset and growth? How can we enable a longer-term investment in someone? This usually results in partnering to identify optionality for them and their shifting needs."

Amy Hubler
Audit & Assurance Managing Director, Future of Work, Deloitte & Touche LLP

Deloitte and PitchBook have collaborated to produce a unique methodology for the ***Road to Next*** series, in order to better analyze a new segment of companies that emerged in the 2010s. Dubbing this segment the expansion stage, the methodology uses investment data restricted to late-stage VC, PE-growth, venture-growth, and private corporate financing, if applicable. In addition, companies must still be privately held by investment firms. In this report, work software is defined as automation/workflow or business/productivity software as codified in the PitchBook Platform.

1: "Powering Human Impact with Technology," Deloitte, Steve Hatfield, et al., January 9, 2023.
2: "2023 Global Human Capital Trends," Deloitte, Kraig Eaton, et al., n.d., accessed February 6, 2023.

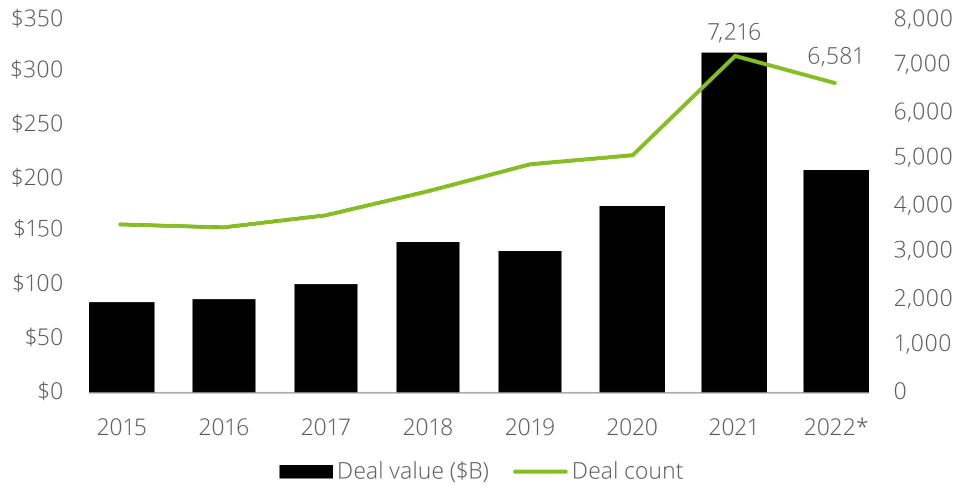
Market trends

Amid general vigilance, work software dealmaking remains resilient

Both general expansion-stage and work software dealmaking notched such lofty highs in 2021—$317.5 billion across 7,200+ completed transactions and $53.0 billion over 1,248 deals, respectively—that any return to tallies closer to historical averages was likely. 2022 saw more resilience than may have been expected, however, with work software accounting for 15 percent of total expansion-stage deal value and seeing a more modest decline in closed financing volume.

The drivers of this resilience are numerous. In any era marked by volatility, both founders and investors turn toward more quickly accumulative business models. This instinct aligns with enterprise software tools that promise to empower existing workforces by enhancing productivity and increasing overall return on investment (ROI). As the cost of capital in general rises due to interest rate hikes, discounted cash flow calculations pull forward the timeline needed for returns. This acceleration also has turned investor attention toward more sustainable growth trajectories, which are more likely found among longer-lasting business-to-business contracts for software tool suites. Last but not least, even amid the onset of market jitters in 2022, many larger businesses and investment firms still had the financial resources for upfront investments that were sizable in the short term but positioned their capabilities or portfolios well for the longer term.

Expansion-stage deal activity



Source: PitchBook | Geography: US | *As of December 31, 2022

> "For emerging growth companies, the challenge may be grappling with degrees of uncertainty or not necessarily having the luxury of significant resources to invest in plenty of preparation, so a key element in our efforts—especially in usage of any automated tools—is asking the right questions to be better able to assess risk levels, even in areas unfamiliar to our clients."
>
> **Heather Gates**
> Audit & Assurance Private Growth Leader, Deloitte & Touche LLP

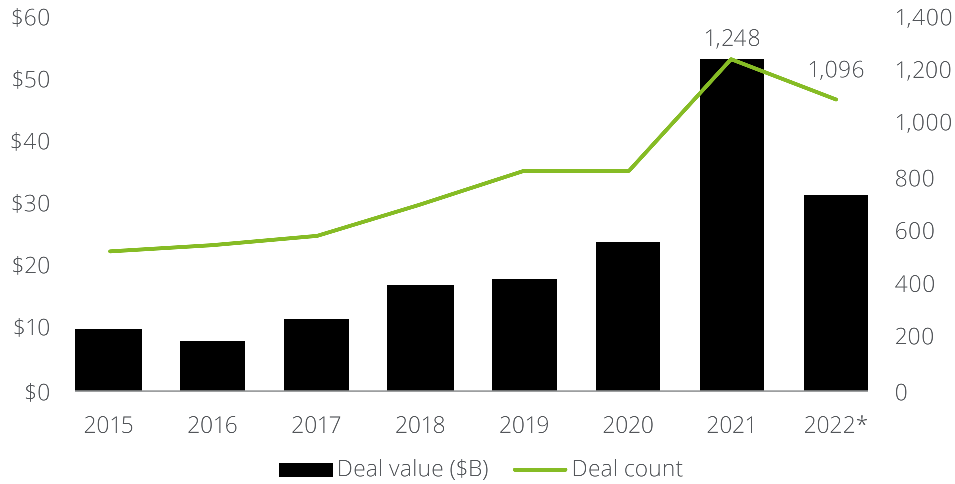
Financing metrics paint picture of growing caution amid capital-rich environment

Median financing sizes broken out by type reveal that venture-growth deals remained steady, barely dipping from $35.4 million in 2021 to $35.0 million in 2022. Other medians did decline, yet only to historically healthy marks. Coupled with post-money valuations remaining relatively high, these financing metrics suggest that amid a relatively capital-rich environment, albeit one characterized by rising caution, work software businesses with the most robust financials could still rake in substantial sums of capital to continue growth. However, this was during a time of choppy public markets and mixed economic results. Much like in recessions past, should a recession hit hard, dealmaking will likely plummet, even for firms with sound business footing.

Building upon incremental advances in underlying tech, work software is poised to quietly yet significantly evolve in the 2020s

Beyond market trends and capital flows, however, work software is not only still reaping the rewards of innovations in business models and underlying, fundamental technologies, but also poised to become even more dynamic and powerful. The ubiquity of software-as-a-service (SaaS) models and their implications on the business and financials sides are well known and documented; the implications of automation, intelligence, customizability, modularity, and security in next-generation work software tools are still being explored.

Work software expansion-stage deal activity

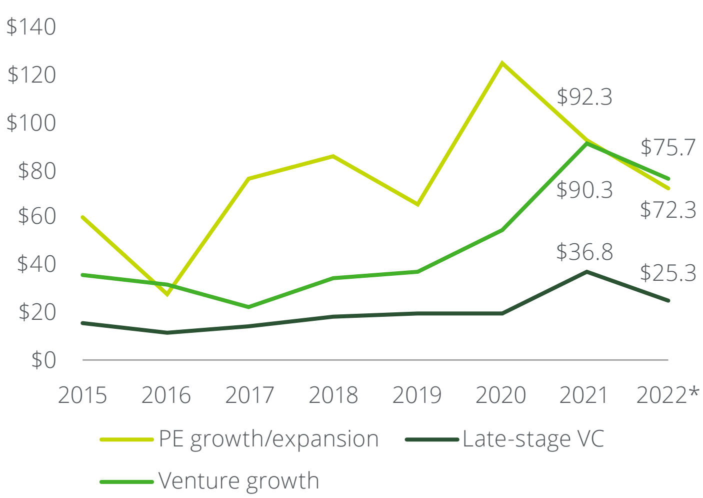


Source: PitchBook | Geography: US | *As of December 31, 2022

New hype around artificial intelligence (AI) capabilities is already surging through the business world, but the reality underlying the hype is worth detailing. Although no-code/low-code tools can be somewhat limiting due to need for nuance and the degree of care required for inputs, they still can help automate very routine processes, thereby improving the appeal of entry-level jobs. Increasing the modularity of different tools so they can apply to more situations can help reduce the burden of detailed preparation for specific clients. In addition, legacy workflows that then are customized by their first users can be more easily passed down to successors after their first round of adaptation. On the predictive side, AI-empowered, intelligent tools can save hours of manual trawling through detailed documents and resources to unearth instances of recurrence.

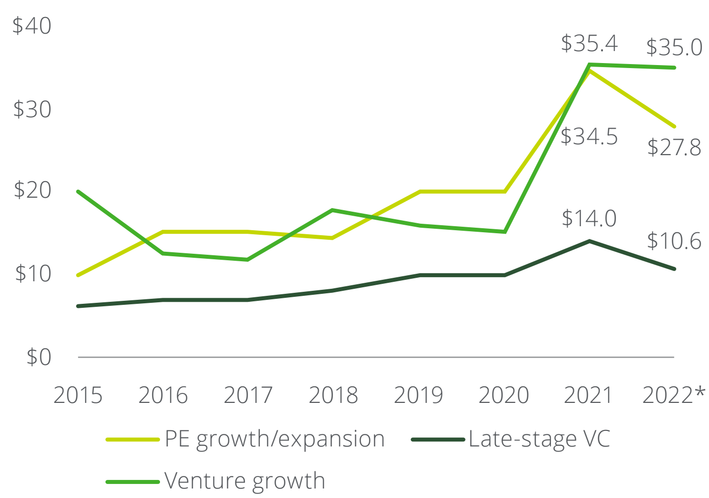
Many other examples are emerging in case studies, and more should be expected. The usual concerns, such as these tools eliminating too many jobs or functions, are proliferating once again. However, historical patterns of technological innovation show that even when jobs are eliminated, new job categories are created, and, moreover, the types of jobs that disappear tend to be the most menial—for example, the manual cutting and pasting of individual strips of text in typewriters prior to digital

Average work software expansion-stage deal value ($M) by type



Source: PitchBook | Geography: US | *As of December 31, 2022

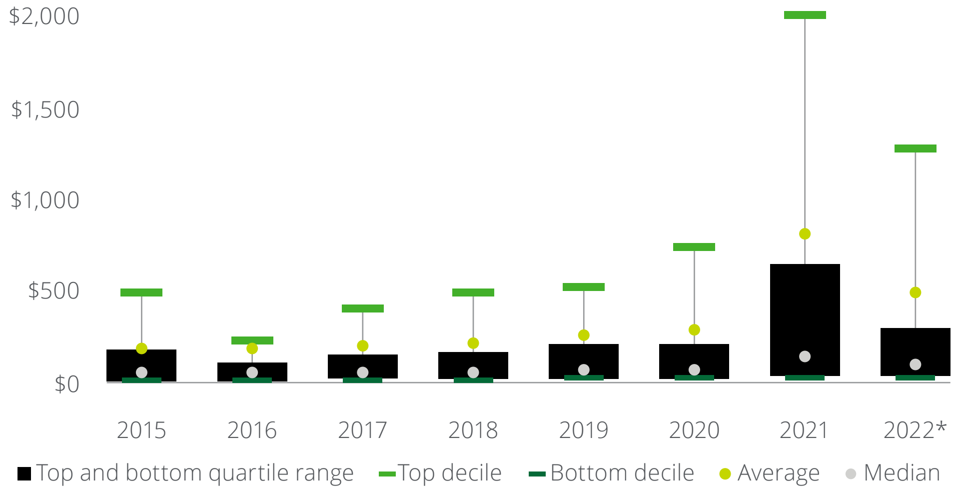
Median work software expansion-stage deal value ($M) by type



Source: PitchBook | Geography: US | *As of December 31, 2022

text editors. The key distinction in this next phase of development is ensuring that heed is paid to adapting to worker preferences and workflow innovation itself. As Deloitte's recent Global Human Capital Trends survey revealed,[3] with work increasingly done across former functional bounds, the automation of segmented routine tasks lends an opportunity to reinvent job titles and organizational structures. This opens up even more potential market niches for work software companies to target. Moreover, many companies are undertaking preparations to do so, given the cues issued by the broader dealmaking market.

Work software expansion-stage post-money valuation ($M) dispersion

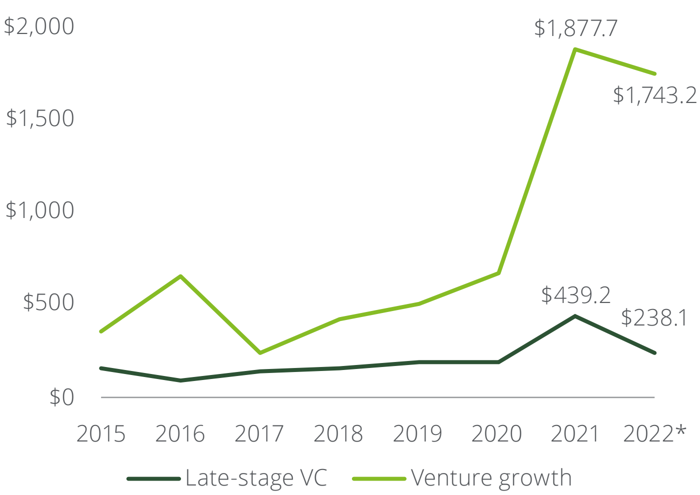


Source: PitchBook | Geography: US | *As of December 31, 2022

"Students hired out of school often do not want to do low-risk, repetitive work. They ask instead about how we could automate those types of tasks. They in turn prompt us to re-examine which types of platforms—such as no-code or low-code tools—could empower them to invest time upfront to create automated solutions that would end up saving them and future hires hours of work per quarter, which adds up over time."

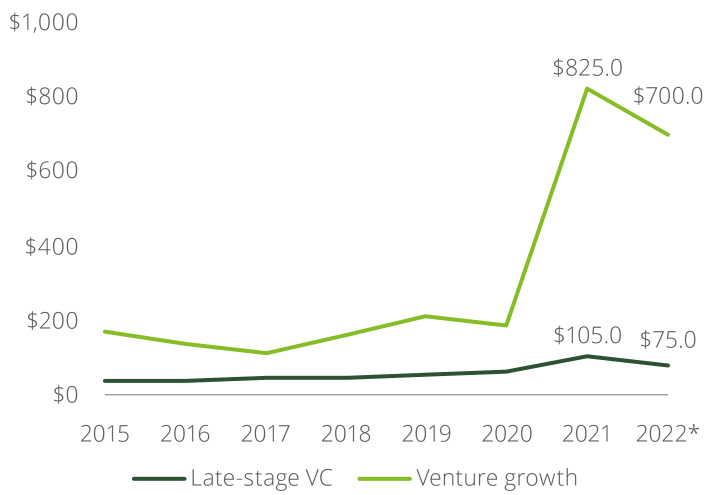
Amy Hubler
Audit & Assurance Managing Director, Future of Work, Deloitte & Touche LLP

Average work software expansion-stage post-money valuation ($M) by type



Source: PitchBook | Geography: US | *As of December 31, 2022

Median work software expansion-stage post-money valuation ($M) by type

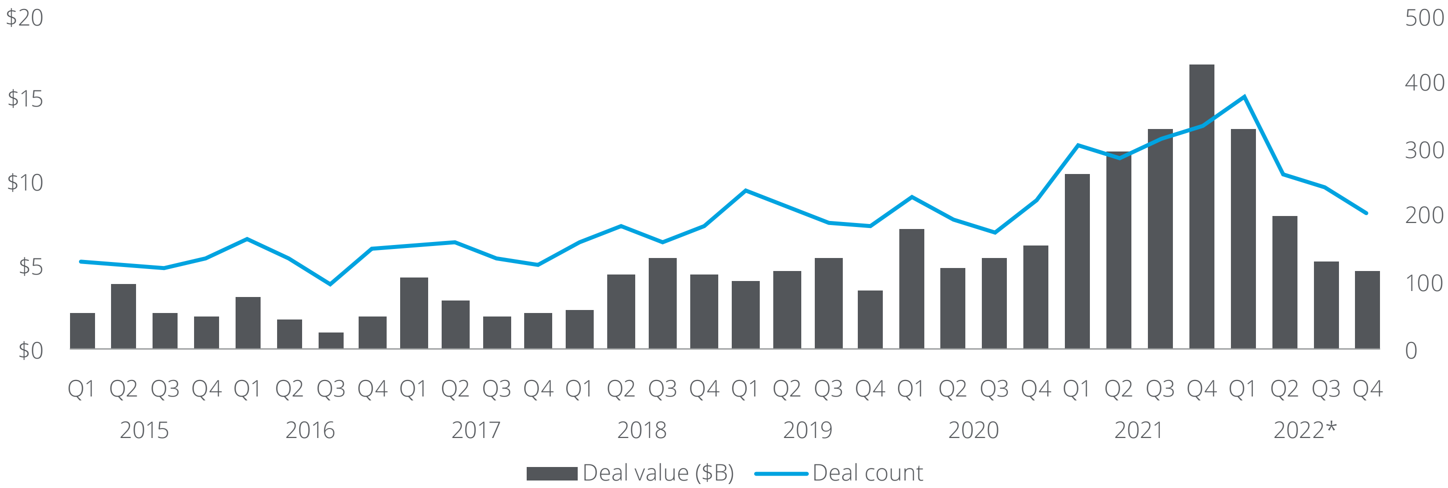


Source: PitchBook | Geography: US | *As of December 31, 2022

3: "Navigating the End of Jobs," Deloitte, Sue Cantrell, et al., January 9, 2023.

Highlights across investment trends

Work software expansion-stage deal activity by quarter



Source: PitchBook | Geography: US | *As of December 31, 2022

Even in the expansion stage, momentum in dealmaking may be slowing across private markets. Yet work software remains at least as popular as it was prior to the bull markets of 2020 and 2021. Moreover, financing metrics reveal that investors are still willing to deploy considerable sums for the most prepared and high-functioning businesses that can demonstrate not only growth rates but sustainable financials. As the crop of expansion-stage work software companies matures, the prospects for ongoing investment activity are consequently higher, given greater financial resources and experienced backing. Even though liquidity has been variable over the past several years—and has slowed recently—dealmaking across work software will likely continue at a moderate pace, thanks primarily to inexorable macroeconomic forces such as lowering overall operating expenses via automation and maintaining competitive edges and economies of scale through AI-empowered workforces and proprietary datasets. Blending these advances in technological innovation with adaptations in workforce preferences and employee empowerment will likely be a priority for work software companies going forward, especially in increasingly competitive labor markets.

15%

In 2022, work software hit its second-highest percentage of all expansion-stage deal value on record.

$100M

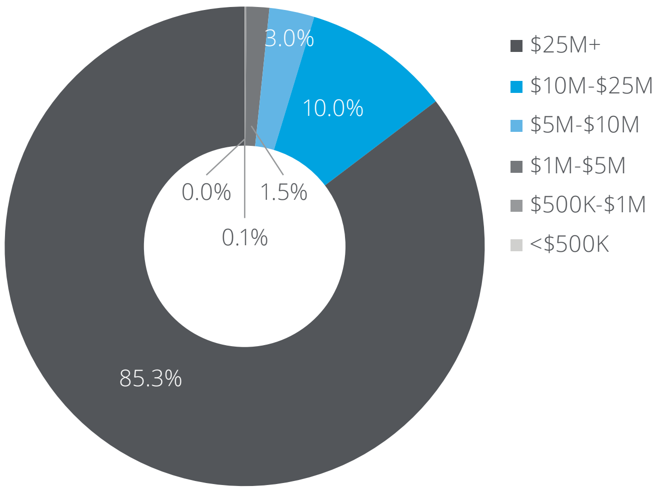
The median exit size via acquisition for work software companies in 2022 was more in line with historical averages.

115

2022 saw the most completed rounds in the $5 million to $10 million range in history, signaling both capital availability and growing caution.

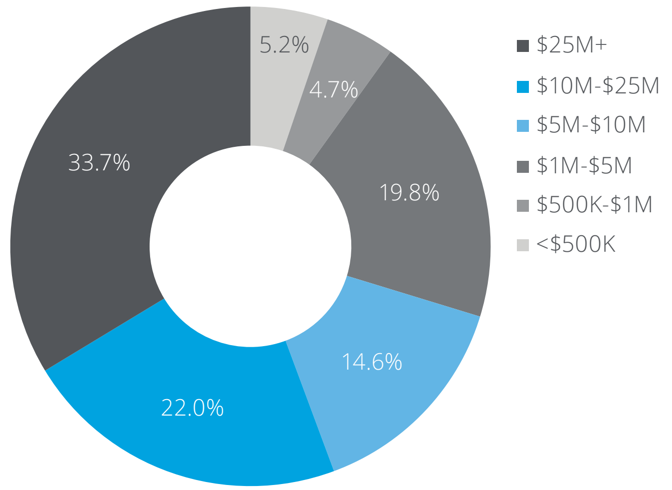
All callouts | Source: PitchBook | Geography: US

Share of expansion-stage deal value by size bucket in 2022*



Source: PitchBook | Geography: US | *As of December 31, 2022

Share of expansion-stage deal count by size bucket in 2022*

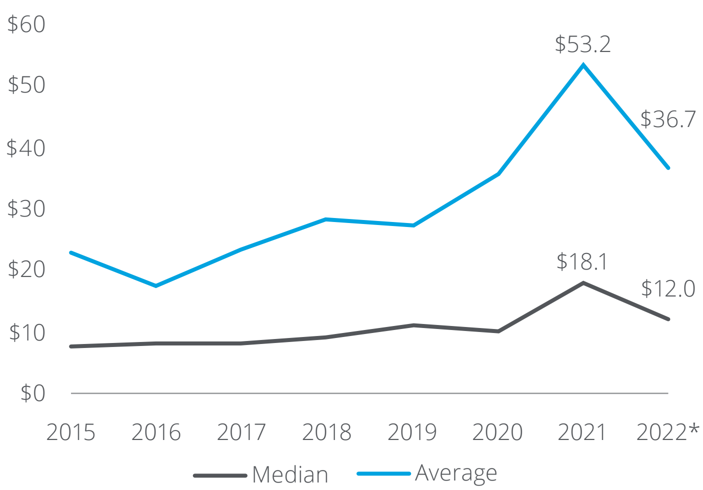


Source: PitchBook | Geography: US | *As of December 31, 2022

"Bringing together working groups that span multiple sectors and client types can help generate not only better processes for workflows but also more diverse, in-depth insights for our clients. We want to bring the best of Deloitte to our clients without being constrained by geographic borders."

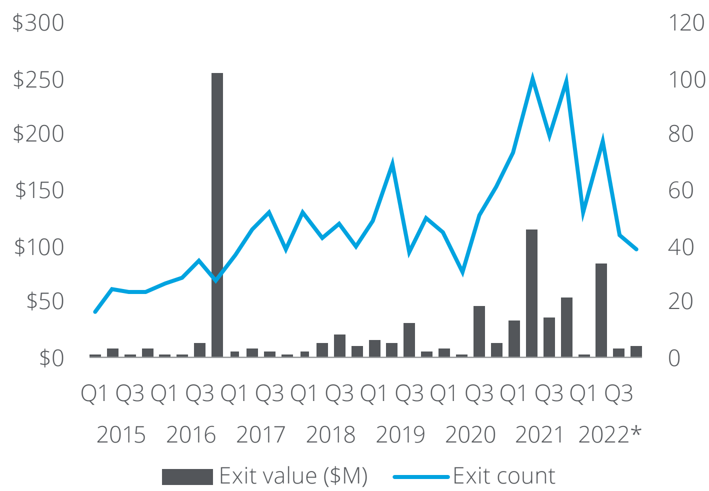
Amy Hubler
Audit & Assurance Managing Director, Future of Work, Deloitte & Touche LLP

Median and average work software expansion-stage deal value ($M)



Source: PitchBook | Geography: US | *As of December 31, 2022

Work software expansion-stage exit activity by quarter

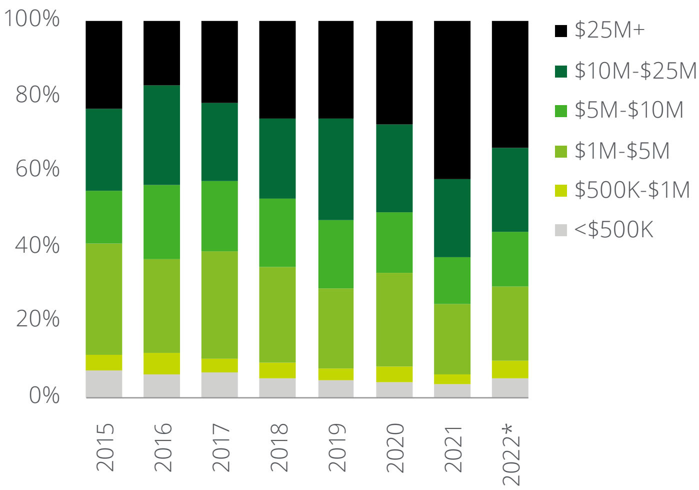


Source: PitchBook | Geography: US | *As of December 31, 2022

"Data and analytics, further augmented by a burgeoning suite of AI-enabled applications, are increasingly a layer of functionality across every department in companies, regardless of sector."

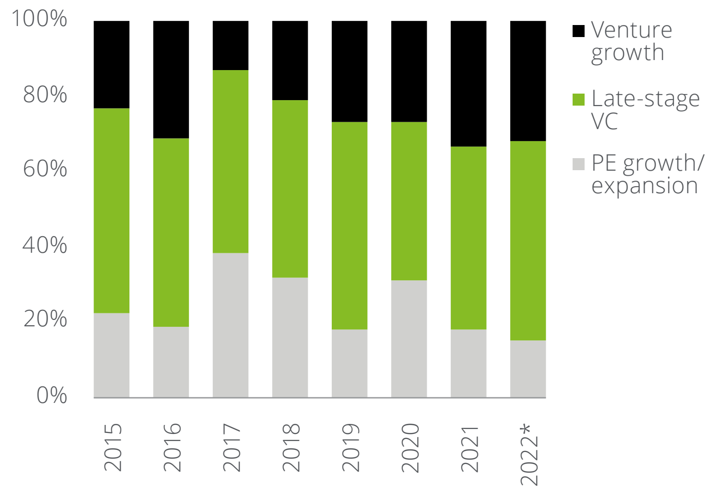
Heather Gates
Audit & Assurance Private Growth Leader, Deloitte & Touche LLP

Share of work software expansion-stage deal count by size bucket



Source: PitchBook | Geography: US | *As of December 31, 2022

Share of work software expansion-stage deal value by type



Source: PitchBook | Geography: US | *As of December 31, 2022

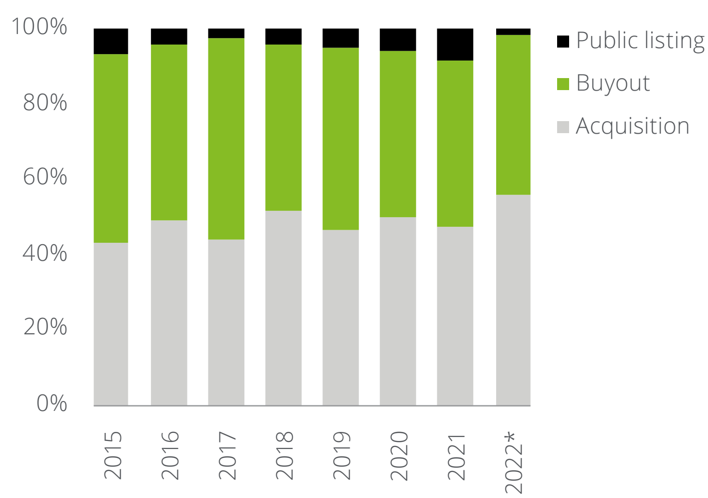
The evolution of work software dealmaking throughout the 2010s provides clues to the 2020s, as companies prepare to navigate choppy markets

Breaking down work software expansion-stage dealmaking in the past decade hints what may transpire in this decade, especially as companies prepare to retrench for any volatility. Initially, venture growth grew proportionally in the first half of the decade, before retreating, only to surge again. This suggests that a cohort of work software companies matured and achieved significant liquidity events, and then another cohort has since matured and grown—of which, many companies exited in the past couple of years. However, the scale of maturation shifted toward the larger end thanks to the availability of private capital throughout the 2010s and the precedent created by the advent of the unicorn phenomenon. Thus, exits also became correspondingly larger, with many opting to go public, given their sheer size and the buoyancy of equities markets until recently.

“Many emerging growth companies that were able to easily raise capital during recent prolific environments are now facing more challenges. However, they also are engaging more proactively in preparations for significant liquidity events that initially delayed public listings or other large transactions due to sheer volatility that surged a year or so ago. Although there have been growing pains, a broader readjustment toward being better prepared has been occurring as well.”

Heather Gates
Audit & Assurance Private Growth Leader, Deloitte & Touche LLP

Share of work software expansion-stage exit count by type

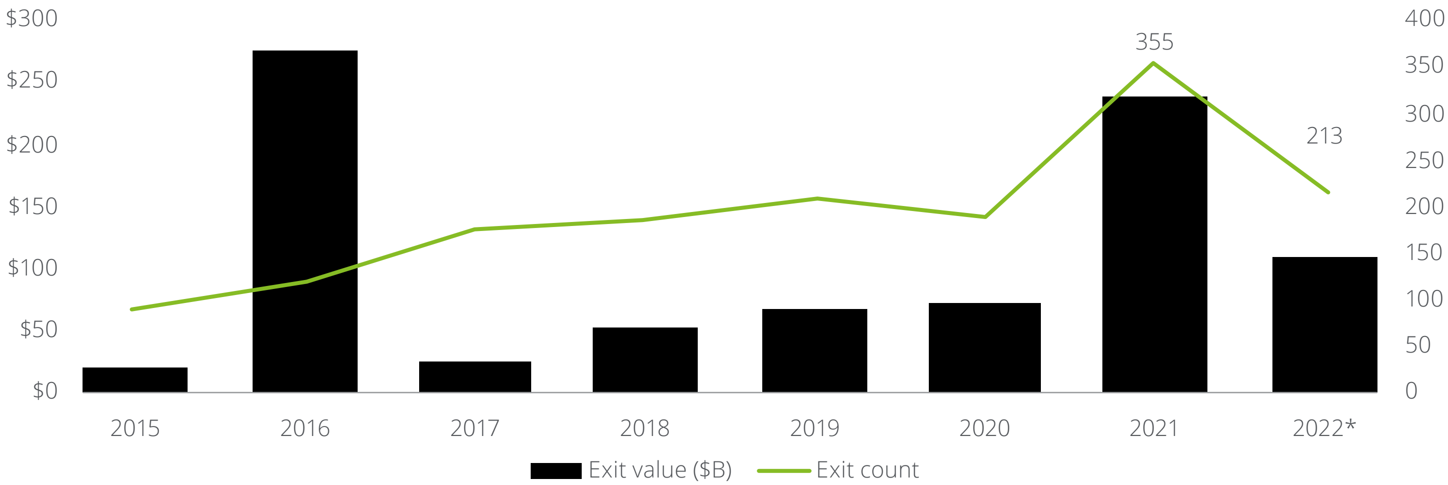


Source: PitchBook | Geography: US | *As of December 31, 2022

"As workflows grow more automated and operated by intelligent systems in real time, ensuring that the correct underlying data inputs align with all relevant parties' data is critical. Not all data collected at a given company's financial level necessarily aligns with what has to be prepared for going public, for example, which means that rendering true process must be able to be flexible in terms of inputs. That goes for other firms in other sectors, too, or really any broader workflow with multiple participants and different approaches to datasets."

Heather Gates
Audit & Assurance Private Growth Leader, Deloitte & Touche LLP

Work software expansion-stage exit activity

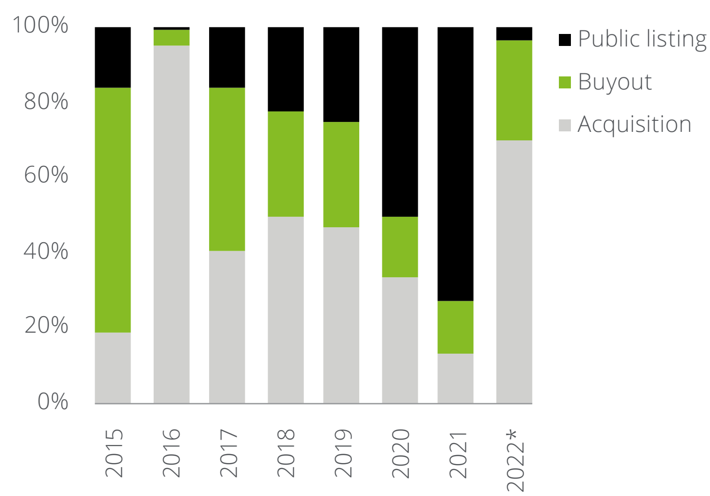


Source: PitchBook | Geography: US | *As of December 31, 2022

What lies ahead from a liquidity perspective?

The current exit window is murky. However, work software companies may face a slightly different climate than others; even during turbulent times, software companies' roadshow pitches detailing how their tools can help companies quickly trim costs and future-proof their businesses remain quite appealing. Strategic acquirers may also grow more active should an attractive balance between moderated private valuations and acquisitive growth be struck. However, market volatility plus concerns around faltering or contrary economic indicators could still extend liquidity timelines, even for relatively well-positioned work software companies with healthy balance sheets. It remains to be seen how early-2023 exit tallies may reflect market sentiment.

Share of work software expansion-stage exit value by type



Source: PitchBook | Geography: US | *As of December 31, 2022

Spotlight: Emphasizing the "human" in human capital

As market trends remain relatively dynamic, qualitative data shows the appetite for innovation among workforces is strong

A significant opportunity exists for work software companies to market their solutions as bridging the gap between ease of use for people at a given type of organization—whether by structure or sector or both—and their current needs. For example, a manufacturer of fencing for suburban homes may be looking to expand into additional product lines, yet may be facing difficulties sourcing the requisite resources for strategic planning and identification of which markets and product types to tackle first. The right work software suite could not only help incorporate supply chain outputs and product suites to identify which new product lines would be the most cost effective to expand into, but it could also review existing processes and identify gaps to more effectively leverage commitments and team members. That final aspect is critical, especially for current enterprises.

Regardless of sector, the foundation of every business is human capital. The current talent market is as competitive as ever but for different reasons than in the past, and it is likely to grow more so due to demographic shifts, changing worker expectations, economic pressures, and emerging novel modes of work. For example, half of organizations that establish and embrace a concrete purpose enjoy better retention, per the Global Human Capital Trends survey.[5] Pairing such strategic adoption with support for a truly diverse workforce—from initial talent pipelines considering nontraditional backgrounds, to ongoing training opportunities for employees looking to shift career paths or acquire new skills—will help companies of all kinds adapt better in a variety of oncoming economic conditions. Accompanying work software suites that can smooth transitions and track progressions along planned strategies will be needed, thus creating new market niches as well, with the end goal of empowering the individuals using these tools to get work done and develop their desired experiences and skillsets.

"The workforce is looking for multiple, diverse pathways to obtain skillsets or progression or both. We are investing heavily in our talent experience, determining how to adapt traditional career pathways to ensure different progressions are possible for multiple backgrounds—even those from outside traditional academic or work backgrounds, such as accounting."

Amy Hubler
Audit & Assurance Managing Director, Future of Work, Deloitte & Touche LLP

5: "Harnessing Worker Agency," Deloitte, Sue Cantrell, et al., January 9, 2023.

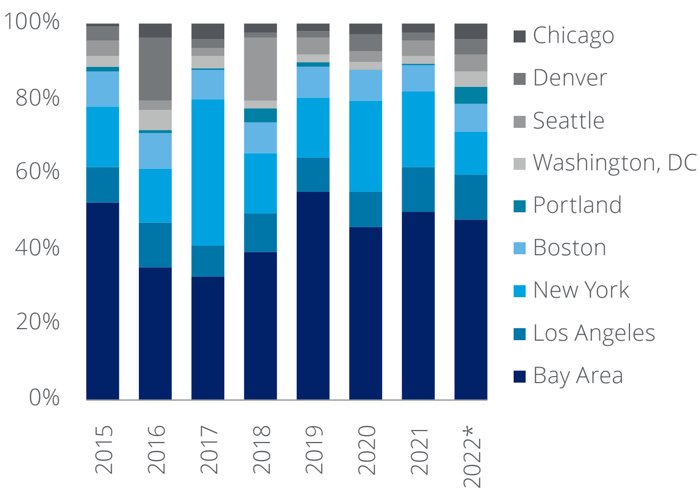
Regional spotlight

Proportional trends in dealmaking across work software remained by and large steady in terms of volume over the past decade, though a slight decline in Bay Area tallies suggests declining market sentiment. In years past, variability in aggregate deal value has been explained largely by outlier deals. However, tracking work software dealmaking going forward, in tandem with traditional geographic setups for companies, is likely to prove more challenging. While full decentralization is currently not the norm for companies, the fact remains that in large part due to the novel responses wrought by the pandemic, many workers remain desirous of flexible remote work options. Furthermore, inexorable rising costs in metropolitan areas have encouraged offices to shift to more decentralized, hub-and-spoke models across broader swaths of suburbia or smaller towns. As a result, there is potential for gradual geographic shifts in not only work software dealmaking but even expansion-stage dealmaking, even though it will likely take some time and remain concentrated primarily among traditional regions, as opposed to metropolitan areas.

"Another key part of building the future of work is determining which hybrid strategy is best suited for a variety of challenging and diverse workflows. The spectrum of preferences is broad, from people preferring a central hub to collaborate and socialize, to those opting to work primarily virtually. Leaders must consider many factors, especially the type of work, when defining an organization's hybrid work strategy. Decentralized structures may work in some situations, but not all, so exploration and flexibility are vital to best position both the people and the organization for growth."

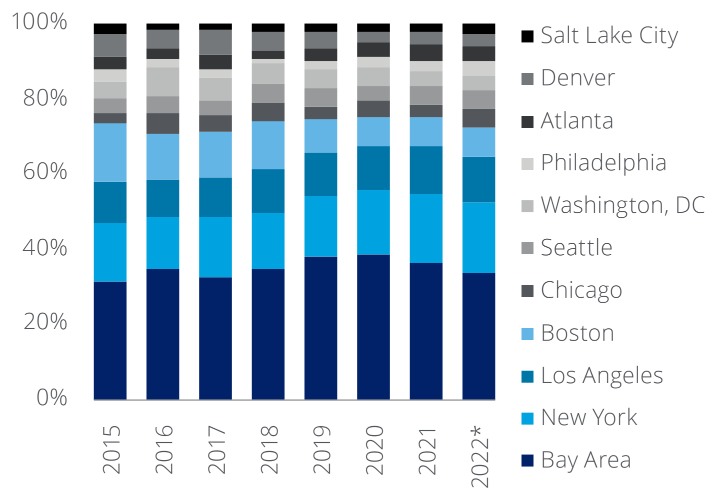
Amy Hubler
Audit & Assurance Managing Director, Future of Work
Deloitte & Touche LLP

Share of work software expansion-stage deal value by top metropolitan areas



Source: PitchBook | Geography: US | *As of December 31, 2022
Note: The metros were selected on the basis of having at least 20 or more completed transactions in work software in 2022 or $1 billion or more in deal value in 2022.

Share of work software expansion-stage deal count by top metropolitan areas



Source: PitchBook | Geography: US | *As of December 31, 2022
Note: The metros were selected on the basis of having at least 20 or more completed transactions in work software in 2022 or $1 billion or more in deal value in 2022.

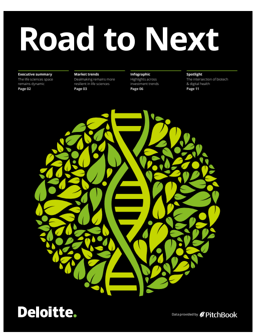
2022 at a glance

Q1 2022
Foodtech
$6.1B
169
deals

Foodtech concluded 2022 with a robust 169 transactions completed, just 20.3 percent below the record tally of 200+ covered in the Q1 2022 edition of Road to Next, but still healthy relative to historical averages. Hurdles remain for fast-growing players within the space, primarily around competition from incumbents and cost of inputs. However, regulatory policies seem primed to evolve even more in favor of novel protein ingredients and decentralized production centers for urban agriculture to help combat food deserts.

Expansion-stage exits plummeted from the heights of 2021, returning to volumes and metrics last seen in the mid-2010s, e.g., the Q2 2022 edition reported a few hundred exits that slowed to only produce 1,381 exits total by the end of the year, a 62.7 percent decline from 2021. Given general market volatility, liquidity prospects seem murkier heading into 2023. Dealmakers may eventually look to acquire as they can strike bargains with companies that saw their valuations get marked down. For example, there are already many rumors of take-privates by capital-rich PE firms. Public listings are likely to remain sluggish until more stability returns to the market.

Q2 2022
Exits
$463.6B
1,381
exits

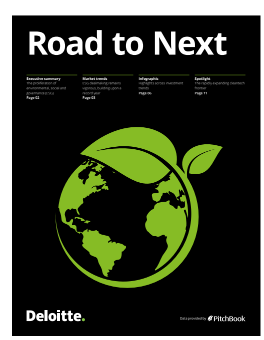


Q3 2022
Life sciences
$22.2B
941
deals

Although life sciences dealmaking declined from prior highs, it still notched the third-highest tally of annual deal value on record at $22.2 billion, up from $12.9 billion reported in the Q3 2022 edition, across 941 completed transactions. Despite hurdles such as supply chain cost increases and customary regulatory barriers, this sector is likely to remain more resilient than others due to longer-term macro factors including patent expirations, approvals of novel therapies, aging demographics, and more.

Environmental, social & governance (ESG)-related dealmaking in 2022 was one of the few arenas of expansion-stage financing activity to grow, hitting a new high for completed transactional volume—full-year figures for 2022 closed in on 460 completed transactions, 40 percent higher than the 330 cited through September's end in the Q4 2022 Road to Next edition. Especially as the global labor market remains volatile, businesses are investing more in retention, training, and innovation across all aspects of ESG to improve longer-term financial and social outcomes in which they are directly involved. Helpful tech solutions are being brought to market to further augment these efforts, including improved measurement of social outcomes, environmental impact, and governance reforms.

Q4 2022
ESG
$23B
460
deals



Looking forward

Any period of downturn, particularly for companies at the growth stage, also poses opportunities for change

At the confluence of work software, current teams, and the pipeline of talent that companies are looking to hire, change is omnipresent. Many workers may be back in offices, but they aren't there as often as they used to be, and sentiment remains firmly in favor of worker empowerment with regard to flexible hours and locations. Otherwise, retention is likely to be a challenge, survey results suggest.[6] However, simultaneously, work centers and building collaborative relationships remain important. Finding a harmonious balance between these trends is possible, but it will require both adept strategizing by executives and investment in tools to empower existing teams and derive insights from such teams' perspectives and intentions to design a mutually agreeable future. Given those pressures, the current volatile dealmaking environment contextualized against the longer-term, broader market and economy, underscore the opportunity to make significant changes. As a result, work software providers are revamping their product and service offerings and reorganizing along novel lines that may turn out to be the workplace, workforce, organizational structure, and operating models better suited for the future, thus enhancing overall productivity and well-being.

"A key consideration for any executive team is to try to assess what your relevant talent pool will look like in the future. After a frenetic period for many teams, given the bull markets of the late 2010s and challenges in labor markets, it is now wise to assess how to better empower existing teams and also appropriately deploy new resources so that one can leverage alternative, distributed teams and specialists where they are most needed."

Amy Hubler
Audit & Assurance Managing Director, Future of Work, Deloitte & Touche LLP

6: "Activating the Future of Workplace," Deloitte, Steve Hatfield, et al., January 9, 2023.

Methodology

Geographical region: United States

The **expansion stage** is defined from a transactional perspective as including late-stage venture or growth financings as defined by PitchBook. The primary industry codes utilized in this report were automation/workflow software and business/productivity software. For this edition in Q1 2023, some underlying methodologies were changed due to PitchBook's methodological changes and incorporation of the new **venture-growth stage**, which will slightly shift numbers yet be more accurate and granular going forward.

Active investors: The number of active investors is calculated by including either investors that have raised a venture or growth fund in the trailing five years or those that have made four or more VC or PE growth investments in the past three years. There is no exclusion on investor type, apart from angel investors.

All investment data is restricted to late-stage VC, PE-growth, venture-growth, or corporate financing types, as defined by PitchBook. **Nontraditional investors** are defined as hedge, mutual, or sovereign wealth funds. All **exits** are defined by PitchBook's primary exit types: buyouts, acquisitions, or public listings, which include direct listings, traditional public listings, and SPACs. The underlying companies are those that have, at minimum, achieved any of the investment data under restrictions.

Company inventory is calculated by tallying the number of companies that achieve either late-stage VC, PE-growth, or corporate financing by year and have not recorded an exit event as of the year in question. Unless otherwise noted, all exits were made by companies that fall under the aforementioned criteria for expansion-stage companies. The number of sellers was based on the count of investors classified as PE by PitchBook within the IPO event.

This report was written in early February 2023. All data is as of December 31, 2022.

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