

PErspective in GOVERNMENT CONTRACTING

A FEATURE EXAMINING THE ROLE OF PRIVATE EQUITY IN THE GOVERNMENT CONTRACTING SPACE.

For PE firms, FY '16 offers a glimmer of hope in the government contracting space – especially in the healthcare and tech industries.



Although the federal budget outcome for fiscal year 2016 remains to be seen, the government contracting industry

continues to find opportunities in the healthcare, technology and defense industries. Specifically, the healthcare and technology sectors are providing some glimmers of hope for private equity firms looking to grow or exit their investments.

Defense retains the largest overall spend – \$200 billion in fiscal year 2014 – although that figure is down by more than a third from 2008. Despite this, private equity firms have never been more invested in the defense contracting space. Between 2004 and 2013, private equity invested more than \$30 billion in 358 U.S. defense and aerospace companies, according to Pitchbook data. However, sequestration fears and budget caps mean that many have held onto their investments longer than usual, delaying exits while waiting for the market to improve, the *Washington Post* reports.

Meanwhile, the Affordable Care Act, as well as legislation passed under former President George W. Bush to modernize the government's aging IT infrastructure, have provided plentiful opportunities for providers of healthcare and more general technology. Agencies across the board are looking to update their systems and improve their systems' defense capabilities. President Obama's proposed fiscal 2016 budget includes \$86 billion for IT spending – a year-on-year increase of 2.7 percent – including \$14 billion for cybersecurity.

These trends have spurred robust M&A activity. Big-name contractors – especially from the defense sector – have acquired smaller healthcare IT companies in order to bolster growth. Last October, defense contractor Lockheed Martin bought healthcare IT company Systems Made Simple, and defense and intelligence firm Booz Allen Hamilton made two healthcare IT acquisitions – the health division of Genova Technologies, which has received \$90 million in HHS business since the passing of the health law, and health analytics startup Epidemico. This comes as part of a larger push by Booz – part-owned by the Carlyle Group – to sell technology and consulting services to the Department of Health and Human Services, the *Washington Post* reports.

“Private equity firms are both buyers and sellers in today's market,” says **Joe Burke, Transaction Advisory Services Partner in BDO's Government Contracting practice**. “Valuations continue to vary greatly based on the level of the government contractor's capabilities and the size and visibility of their customer contracts.”

Other contractors have also been snapping up smaller technology companies for their lucrative federal contracts. In March, for example, state Medicare claims processor Maximus acquired technology contractor Acentia for \$300 million from private equity firm Snow Phipps Group in order to grow its federal healthcare IT contracting footprint. Over the last two years, Accenture and ManTech International acquired ASM Research and Delta respectively – both of which had a task order in the Department of Veterans Affairs' \$12 billion contract to modernize its electronic health records, the *Washington Post* reports.



Cybersecurity is another area of growth, attracting significant investment from private equity companies. Bain Capital recently acquired Blue Coat Systems for \$2.4 billion with the goal of returning it to the public markets. Private equity firms spent \$191.9 billion globally on data security firms last year, up from \$170 billion in 2013, according to the *San Francisco Chronicle*.

The number of defense company exits we see in the next year will hinge a lot on whether Congress increases military spending. But whichever version of the budget passes, private equity companies will likely see continued opportunity in the healthcare and technology spaces.

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