Notes on TARGETCO

DRAFT for DISCUSSION

Month DD, YYYY

Summary

- An interesting company with a nice niche. It is indeed painful for Program Offices/Procurement Executive Offices (PEOs) to execute without something like what TARGETCO offers. Specifically, Program Offices and PEOs are required to submit financial reports monthly at a granular level. The challenge is that they don't get numbers from the financial systems until right before the deadline and, when they get it, the data is not in a form that matches what they must report. The result is an error prone fire drill to comply. Further, without a solution such as TARGETCO provides Program Offices and PEOs are forced to be reactionary instead of proactive.

- TARGETCO's bias towards services and paid development follows an old tried-and-true model, though it will limit their value in the long term. There is significant upside by professionalizing operations, upgrading customer account development, adding a sales manager and team, evolving the mix of offerings to be more product-based, subscription priced, and SaaS delivered, and building out new products to license back to the installed base.

Business Model: 15.1% of revenue comes from software and related maintenance (traditional pre-cloud Commercial Off-The-Shelf (COTS) software delivered on premises approach) which leads to 21% of revenue that comes from government funded software development likely owned by the government (GOTS), and then that leads to the 64% of revenue from services by badged, on-site (embedded) staff to provide highly customized support, training, maintenance, and enhancements.

Key Points

- Government customers are notorious for their insatiable appetite for ongoing customized software development, maintenance, support, and refresh which is expensive for the government and lucrative for TARGETCO as there is likely no other source for this work and TARGETCO rates can be usurious (unless contracted as Cost Plus Fixed Fee (CPFF)). Once entrenched, the odds of staying under contract are extremely high.

- How portable across customers and markets is the software functionality developed from funding provided by specific customers?

- TopVu is another company that sells technology solutions into DoD Program Offices to help with contract management. Compusearch (now Unison) acquired TopVu. Based on that experience, there is no doubt that the opportunity for automation to drive efficiencies and to integrate work activities in defense agency Programs and PEOs is large, and TARGETCO appears positioned to capitalize.

- **Market**
  TARGETCO is an old "**Tech-Enabled IT Services**" business. How long will this model be attractive to the market? DoD customers like having their own applications and are not fans of software products (that, in their view, hold them hostage) or SaaS platforms (that may lack customization for perceived unique needs) and the security they crave. So, likely there is plenty of runway for this type of business model in TARGETCO's core market (Air Force and Army).

  o **WHAT:** TARGETCO provides tech-enabled IT services, i.e., IT application services to develop, support, maintain, extend, etc. custom application software built upon a base of licensed core foundation software (CCaR and PRTM).

    NOTE: There is very likely plenty of opportunity to add new products that program offices need and are complimentary/synergistic with their current offerings; including (from experience with TopVu):
    - Managing Foreign Military Sales (manual today and resource-heavy; a MAJOR source of funding for more mature programs).

    - Manage Prime and Subcontractor performance more closely.

    - Streamline maintenance/sustainability of deployed resources (major pain and very manual).

    - Personnel management (who's working on what for how long - which is important at the PEO and command levels as they shuffle resources around).

    - Supply chain visibility and risk management (e.g., foreign influence).

    TARGETCO's 100$^+$ consultants that are on site are ideally positioned to help identify opportunities to exploit such as those listed above, though it takes

work to get them to help.

- o **WHO:** TARGETCO customers are acquisition managers (or the Prime Contractors who support them) in large, complex government (principally air force and army) programs (think fighter planes); It would be good to see a stratification of the market from the largest and most complex Air Force and Army programs to the smallest and least complex to see where in the continuum TARGETCO plays. Most likely they play in the upper part of the middle market just below the very top which have the needs and resources to justify their own custom development of similar software tools and systems. The smaller and less complex programs do not need the sophistication provided by the TARGETCO solution.

- o **WHY:** TARGETCO provides Program Managers and PEOs with their own proprietary version of a cost and requirements management, reporting, and control system that is fully supported by embedded TARGETCO staff; the system is secure and easy to work with (e.g., compared to ERPs and other alternatives, such as custom systems built from scratch).

  Further, Program offices and Procurement Executive Offices (PEOs) are required to submit financial reports monthly at a pretty granular level. The challenge is that they don't get the data needed from their financial system until right before their deadline and when they get it, the reports don't match what they have to report which leads to an error prone fire drill to meet the reporting requirement. The TARGETCO suite solves this problem.

- • **Market Potential**
  Air Force and Army: [DoD services are organized into Commands](#) that have Procurement Executive Officers that oversee Programs. While only a few major new programs are launched every year, only a few programs end every year, and the vast majority are in sustainment mode. Likely a third of the programs are large enough to solve the problem on their own or small enough that they don't need a solution.

  Here is a way to dig-in to the programs to target:
  - o 3 AF Commands with 16 PEOs each with an average of about 10 Programs each: [Air Force Acquisition Organizations.pdf (af.mil)](#)

- 10 Army Commands supporting 12 PEOs each with an average of about a dozen programs: The U.S. Army's Command Structure; PEOs - USAASC (army.mil)

- 10 very big program offices in PEO Aviation: PEO Aviation | The United States Army

- Mission areas for PEO EIS (7): Programs A-Z | PEOEIS (army.mil)

- Programs underneath them (36): Programs A-Z | PEOEIS (army.mil)

Army's PEO EIS owns all business systems for Army and has tried for 10+ years to build something like the TARGETCO solution and failed. The program was initially called AcqBiz. It went nowhere and budgeting was pulled a few years ago. It may have changed names and Army may take another swing at it, but odds are that TARGETCO could be a winner here.

Navy: NAVAIR built their own GOTS solution on top of the Microsoft platform. It's Navy-specific and has not been widely adopted outside of Navy and a few Army PEOs, but it will make sales into Navy very challenging since it's 'free' (note that NAVAIR spends $10M+/year maintaining it, but the expense comes out of NAVAIR's budget so it is essentially free to program offices).

Intelligence and other Defense agencies: The agencies that have significant involvement in building things are of interest: MDA, NRO, DARPA, Washington Headquarters Services, CIA, NSA, and DISCA. These targets will require competence and capacity working in cleared space that are difficult to manage if the company has no experience along those lines already

Civilian: While few civilian agencies have programs as large and complex as those in DoD, TARGETCO mentions early interest in going beyond Air Force and Army. Here is who I'd target along these lines DHS, DoE, DoT, State / USAID, GSA, and HHS.

Market Potential Summary:

- o The best growth opportunities are likely in the 60 existing installations

- o There may, conservatively, be a TAM of ~300 of which TARGETCO currently has penetrated 60.

- o It appears that TARGETCO has yet to even begin to develop a system of proactive sales. Congratulations to them for getting as far as they have with no system of sales but just think about the potential with a high-functioning sales organization.

- **Sales**
  The sales strategy in a business like this is usually to:
  1. Deliver to current customers with excellence
  2. Get current customers to use their system maximally
  3. Sell all you have to every customer
  4. Find and close on all follow-on opportunities to deliver additional value at existing customers
  5. Add new customers with ample potential

Service providers usually fail to manage even their largest accounts like businesses of their own with enormous growth potential to accomplish the second, third, and fourth bullets above. Along these lines:

- o Does TARGETCO have Customer Managers with goals to accomplish the above for assigned customer(s)?

- o Do assigned Customer Managers have performance strategies, goals, plans, and incentives?

Program offices and PEOs are very tribal and difficult to penetrate. Prime Contractors often rule the roost. Mandates from leadership help, but only so much since they think of themselves as islands of sanity in a sea of bureaucracy. It's normal for staff to move from program office to program office and TARGETCO seems to have leveraged this to get new logos. Without references incumbents trust, it's almost impossible to get in the door.

To address this, TARGETCO should hire/retain advisors who come from the other government programs/branches/agencies it seeks to penetrate to do what those

on their team from Army and Air Force have helped them do in the way of penetration.

The company should also hire a professional Federal Sales Manager to set up and manage a system of proactive business development and sales. This could be on a fractional basis initially with the objective to set it up and run it until it becomes core to the business and fully functioning.

Number of salesmen operating at full capacity should be a key metric, but TARGETCO seems to have no salesmen! New sales seem to come exclusively from referrals and customers moving to new jobs. Otherwise, revenue growth comes only from doing more with existing customers.

Are PMRT and CCaR licensed separately? Likely not, but if so, what is license, maintenance, support and services revenue for each over time?

- **Contracts**
  Does TARGETCO have a GSA schedule and if so, when does it expire? How about GWACs?

  Do they have a direct contract with Air Force, Army or other agencies? If so, when do they expire, what are their ceiling levels and how much room is remaining?

  Do they include CLINs for software as well as services and development?

  Do they have contracts with Primes and if so, which ones?

  Are the functional capabilities shown on P. 15 sold and delivered separately or do they all come with CCaR and the chart is to simply show who in the customer organization uses which functionality?

  If sold separately, what revenue have they gotten, and do they expect to get, by function?

  What is meant by mandated for use (by Air Force and Army on P. 8). Is this a basis for "sole source justification"? It would be nice to see the actual mandate wording. It would also be interesting to explore why, if it is a mandate, only 60 programs use TARGETCO and how those that don't avoid doing so.

What is the contracted sales backlog, including option years that have a high probability of being picked up; (i.e., want to see a waterfall chart depicting the timing of contracts and when they are up for renewal).

Much of TARGETCO business appears to be sole-sourced.
- What experience does the company have competing when necessary?

- Do customers get special status credits for purchasing from TARGETCO (e.g., Small Business, Veteran owned, etc.)? if so, will any of these credentials expire (e.g., small business) and what will happen to sales as a result?

- What percent of TARGETCO sales are direct to the government vs. through Prime Contractors. When the sale is through a Prime do embedded TARGETCO staff have permission to work directly with government personnel or are they walled off?

- **Delivery**
  - **Is this correct:** Customers license core foundation software that they then pay TARGETCO to configure, customize, enhance, and support. The net result is a greater work that the government owns but that only TARGETCO can maintain and support.

  - As such, TARGETCO principally delivers IT Services. DoD likes to hire and retain embedded IT service providers as opposed to licensing software or SaaS solutions. ==The constraint to growth in an IT services business is usually the rate at which the company can recruit, hire, train, deploy, develop, and retain people== to deliver their services on target, on time, and on budget.

  - Given TARGETCO technology is proprietary, new employees need training which takes time and makes attrition very expensive.
    - What is the source and age of hires (fresh out of school, experienced, from military?)

- How long does it take to train new employees to be fully productive?

- Why do employees choose to continue working at TARGETCO given limited promotional opportunities and no performance bonuses (per Glassdoor). E.g., do many have military pensions?

  o What is the average Net Services Revenue Per Direct Hour (i.e., the effective hourly billing rate realized)?

  o P. 37: Do customer support personnel work with one customer or across customers?

  o Do embedded staff do their own billing and collections or are billing and collections centralized?

  o P. 7:
    - Does every one of 60 installations have embedded support and maintenance of its own code?

    - Is the right to use TARGETCO software tied to an organization, a CPU, a generic user seat, a named-user seat, or other?

- **Management**
  o It's fabulous that several top team members come from the market the company serves. This is the best way to penetrate a market.

  o On the other hand, no one on the top team seems experienced in leading a maturing operation.

  o Why do the owners really want to sell now? If they don't sell, will the business hit a wall? When? Why?

- **Technology**
  o In what language are the applications programmed?
  o Are there functional and technical architecture schematics to examine?
  o Is there technical debt?

- o Is there a play to offer CCaR and PMRT functionality as higher order packaged application software products or on a subscription basis and delivered via SaaS?
- o P. 32.:
  - To what extent are bottom three rows (AWS, CLOUD ONE, DISA IAP) activated at TARGETCO installations?
  - It looks like this architecture may be a relatively new modernization but has there been uptake from the user base and how is it being received by new prospects/customers?
  - Specifically, how cloud-activated are the top and third layers (CCaR, PRTM) and where does the second layer (ADSB) come from?

  - P. 35: mentions PRTM Cloud Re-platforming. What does this mean? Is it not already operating in the cloud or is it that it needs to be redone to work well in the cloud?

- **Financials**
  - o Good growth, though it slows in '23 relative to '22 and '24; is there an explanation for this?

  - o Great margins, though it suggests they may not be investing enough in growth.P. 59: Are CPFF legacy contracts? I.e., TARGETCO doesn't prefer to do CPFF work, does it?

  - o P. 60: What adjustments have been made to financials?

  - o P. 61:
    - Cash is lower in '22 than in '20 even though sales are up 40$^+$%. Cash was especially low in '21 ($754K). It would be helpful to see a cash flow statement to better understand what's going on.

    - Why does the balance sheet not reflect the value of software assets? Does the company actually own the software?

- **Recommendations**
  - o Hire a Chief Sales Officer to design, build, run, and manage a sales team and campaign to secure new customers.

- o Evolve price list to charge for products, not just services, including on a SaaS/subscription basis with bundled support and maintenance.

- o Repackage and promote offerings to be attractive using a SaaS delivery model and migrate new prospects and existing customers to SaaS/subscription arrangement.

- o Assign, develop, guide, and govern Customer Account Managers to develop multi-year plans to
    - Deliver with excellence
    - Extend and expand current contracts
    - Find new nearby opportunities to deliver additional value

- o Put together an advisory board of retired generals to help attract new customers and improve the offerings.

- o Develop a partner program to optimally engage with Prime Contractors in light of the fact that significantly sized and complex program offices are almost always actually run by primes more than military leadership.

- o Put in place a planning, budgeting, and performance incentive systems to motivate and reward those leaders in the company who drive growth.

- **Other Notes**
    - o In the Fed space, services provided by on-site consultants and custom developers are more like recurring revenue than traditional professional services, though at lower profitability. Such revenue sources rarely go away (just as subscription customers rarely churn) so they should be given more credit than usual.

    - o It is reasonable to pay a premium with the assumption that the product mix (e.g., addition of more products, upgraded packaging and pricing) will improve both top and bottom lines.

    - o To maximize value, TARGETCO should proactively migrate from exclusively services/custom development-led to more and more software/subscription-led. So doing will require a major cultural shift that will primarily fall on Sales/Services, but also will heavily impact the culture and mindset of the entire company, including Customer Success, Product Development, and Product Management. The migration will be

particularly challenging since the leadership team is likely entrenched and vested in their current approach. Given their success to date, it will take thoughtful leadership to motivate and navigate the required change.

- o The company CEO needs to be open and driven to grow as an executive in charge of maturing operations of an evolving software business. The question is whether the sitting CEO is the right person or if a new talent needs to be installed.

- o An acquirer that doesn't know the Fed marketplace well won't have the experience to guide TARGETCO properly (or know when they're being lied to). The solution is to install an executive chairman who can dedicate 1-2 days/week to working with the team on the transformation.

- o It would make sense for Unison to acquire TARGETCO. However, there is little interest given the TARGETCO business model is to sell services which Unison sees as a drag on their model which is to sell product.