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## Growth Equity Case Study – 2-Hour 3-Statement Modeling Test (Atlassian)



You are working at a technology-focused growth equity firm that is considering a \$2 billion minority-stake equity investment in Atlassian, an Australian software company that creates products for software developers.

The company is based in Sydney, but it's incorporated in the United Kingdom and is publicly traded on the NASDAQ in the United States, with offices all around the world.

It is best-known for its issue-tracking and project management application, Jira, its team collaboration and wiki product, Confluence, and Trello.

The company has over 130,000 customers and has been transitioning from a perpetual-license-and-maintenance model to a Software-as-a-Service (SaaS) subscription model.

Unlike other enterprise software companies, Atlassian does **not** employ commissioned sales reps, but instead relies on marketing its products via indirect channels, such as free trials on its website. It has no plans to change this strategy.

As a result, the company spends between 40% and 50% of its revenue on research & development, with only 15 to 20% going to sales and marketing – the opposite of a standard software company.

Atlassian earned \$874 million USD in revenue in its most recent fiscal year, which represented growth of 41% over the prior year and a 3-year revenue CAGR of ~40%. Its Operating Income (EBIT) was negative in FY 18 but had been positive before the IPO in FY 16.

Your growth equity firm is interested in Atlassian because the management team has proposed a potentially lucrative strategy: they want to use the \$2 billion of capital to continue acquiring high-growth software companies and rolling the products of these companies into their own lineup – similar to their Trello and OpsGenie deals.

By doing so, the company immediately gains customers, talented developers, and cross-selling opportunities without spending anything on a traditional sales team.



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In this case study, you will analyze the company from the perspective of a growth equity analyst, create financial statement projections, calculate the potential returns for your firm, and then make an investment recommendation.

Please use the following assumptions and complete the provided Excel template. You have **two (2) hours** to complete this task and make your recommendation:

### **Part 1: Review the Data (Suggested Time: 15 Minutes)**

Start by taking a few minutes to review the key extracts from the company's most recent 20-F report and the article describing its strategy. **Do not read every single word – skim these documents to get the main points in 10-15 minutes.**

We have simplified and consolidated the financial statements to facilitate the modeling process.

### **Part 2: Project the Revenue, Expenses, and Financial Statements (Suggested Time: 40 Minutes)**

Assume that the Subscription Renewal Rate declines to ~90% over 5 years due to the price increases, and assume that New Customer Billings increase by 50% initially and decline to 45% growth, 40%, and so on each year after that. The % of Subscription Billings Recognized as Revenue each year should increase to 70%.

Assume that Perpetual License Revenue Growth declines to 10%, keep the Maintenance Renewal Rate at 90% with 2.5% annual price increases, and assume that Maintenance Billings from New Customers equals 50% of Perpetual License Revenue, declining to 46% over time.

Maintenance Billings Recognized as Revenue can rise from 46% to 50%, and Other Revenue will grow at 50%, declining to 30% over the holding period.

With the Expenses, assume that Cost of Revenue % Standalone Revenue declines slightly from 15% to 14%, that the number of R&D employees is ~2.8x higher by the end, and that fully-loaded costs per R&D employee increase by ~35% by the end.

The effective tax rate, based on corporate rates in the U.K., should be 19% in the first two years and 17% after that.

For the rest of the assumptions, use your judgment and follow historical trends or use averages if there are no clear trends.



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### **Part 3: Project the Acquisitions, Debt, and Taxes (Suggested Time: 30 Minutes)**

Year 1 should reflect the \$295 million OpsGenie acquisition the company has already announced; acquisition spending can then rise from \$700 million to \$775 million by the end.

Follow the numbers already input into Excel for the Amortization of Intangibles and Purchase Price Allocation for each acquisition. This data comes from similar historical acquisitions.

The average revenue multiple for acquisitions is 20x, and the acquired companies initially grow revenue at 100% per year, declining to 90% growth, 80%, and so on. The initial EBIT margin upon acquisition is 10.0%, rising by 2.5% per year after that.

Atlassian has Convertible Bonds that carry a modest Cash Interest Expense; the company must also amortize the Debt Discount and Issuance Fees until maturity. Assume a 5-year maturity and fill these out.

In the Tax Schedule, assume \$150 million of initial off-Balance Sheet Net Operating Losses (NOLs) and calculate Book and Cash Taxes based on that.

### **Part 4: Link the Statements, Calculate the Returns, and Summarize the Model (Suggested Time: 20 Minutes)**

Next, finish projecting and linking the statements based on your revenue and expense projections and the schedules above. Set the Stock-Based Compensation add-back on the Cash Flow Statement to \$0 to count SBC as a true cash expense.

Assume that the \$2 billion equity investment takes place at the end of Year 1 (FY 19), and calculate the IRRs and money-on-money multiples for possible exits in Years 3, 4, and 5.

The initial revenue exit multiple will be 20.0x, falling by 1.5x per year to reflect slowing growth. Assume that the initial equity investment is made at a purchase revenue multiple of 20.7x.

For reference, when Atlassian first went public in December 2015, it traded at revenue multiples between 15x and 20x; after that, it fell to the 10-15x range through 2017, and then rose to the 20-25x range over the past year.

Financial information for Atlassian's peer companies (other high-growth, publicly traded enterprise software companies) is shown below:



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Company Name:	Market Cap (\$ Millions):	Revenue Growth in Most Recent Fiscal Year:	Projected Revenue Growth Next Year:	Revenue Multiple Based on Most Recent Fiscal Year:
ServiceNow, Inc.	\$33,445.8	40.0%	29.2%	13.3x
Splunk Inc.	\$17,519.7	38.6%	24.1%	10.3x
Zendesk, Inc.	\$6,819.6	38.3%	31.6%	12.4x
New Relic, Inc.	\$5,318.2	35.0%	26.2%	12.1x
Workday, Inc.	\$36,647.6	30.8%	25.1%	13.9x
Nutanix, Inc.	\$8,985.5	27.9%	20.1%	7.3x
Dropbox, Inc.	\$9,187.4	27.1%	15.7%	6.3x
SolarWinds Corporation	\$5,126.5	25.1%	14.6%	8.7x

Fill out the summary at the top and the sensitivity tables at the bottom based on this data and the rest of your model. Use your judgment for the ranges of the sensitivity tables.

**Part 5: Make an Investment Recommendation (Suggested Time: 15 Minutes)**

Based on the data above and your financial model, recommend for or against this \$2 billion investment in Atlassian. Your firm is targeting IRRs of 20-25% in the base case, over 30% in more optimistic scenarios, and a minimum IRR of 10% in downside cases.

**Note that you must give a definitive “Yes” or “No” answer.**

Limit your answer and explanation to **1 page or less**.