FOUNDER THESIS CUBE CAPITAL

ISSUE 03

THE PREPARED FOUNDER PREMIUM · POST 3 OF 5

The Discount You Never See Coming

Twelve categories of value reduction that buyers apply before any offer is made, and before most founders realise it is happening

Thesis: The multiple a buyer offers is not shaped by the negotiation. It is shaped by a shadow pricing process that runs months before a term sheet, against a set of signals most founders were never told to manage.

A deal team at a North American strategic acquirer sits down with their investment committee four weeks after signing an NDA with an Australian software founder. The business they are presenting is genuinely good: fourteen million dollars in ARR, growing at twenty-two percent, a product with strong customer satisfaction scores and a renewal rate that, at the headline level, looks competitive. On the measures the founder had spent years optimising, the business looked ready.

The deal team presents two numbers. The first is the business's ARR. The second is the multiple they are prepared to apply to it. The gap between where the founder expects that multiple to land and where the deal team has placed it is not the result of a negotiation that has not yet happened. It is the result of twelve categories of structural discount that have already been applied.

The investment committee approves the model. Three days later, the founder receives a term sheet.

She thinks the process is beginning. The process finished three days ago.

01 The Shadow Process: Internal Underwriting Before The Term Sheet

For founder-led Australian software businesses in the $10 million to $50 million revenue band, this is the part of the market where companies are often large enough to attract serious cross-border interest and still small enough to carry dependencies the founder does not realise a buyer is already pricing.

In Australia, this is also the band where companies often arrive at real buyer relevance before they have institutionalised pricing discipline, contract architecture, second-line leadership, or cohort reporting a buyer can actually underwrite.

Not every acquirer runs the same process. The buyers most active in Australian mid-market software include serial consolidators, PE-backed platforms acquiring for revenue scale ahead of a capital event, and strategic acquirers buying for product or market integration. Their risk models, discount weightings, and tolerance for complexity all differ.

Constellation Software is worth naming specifically, because it has been more transparent than most about how it buys. It looks for a number one or number two competitive position in a defined niche vertical, mission-critical software used by hundreds to thousands of customers, limited competitive intensity, and operational capability that survives without the founding team. Constellation is not evaluating quality in the abstract. It is underwriting fit against a very specific thesis. A business that does not match that thesis is not discounted. It is simply not acquired.

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Where serious acquirers converge is in process. Each runs a visible engagement alongside a parallel risk model. The visible process involves meetings, information requests, and management presentations. The parallel model is invisible to the founder. It begins at the first document, sometimes at the teaser, and by the time a term sheet arrives, it is largely complete. The offer is not an opening position. It is the output of that model.

The shadow process prices twelve categories of risk. Some correspond to the levers examined in the previous issue, taken further into their mechanics. Others appear nowhere in a standard management dashboard. None are disclosed to the founder as a line item. They arrive compressed into a number.

I think of that number as, in effect, the buyer's silent discount model: a reduction layer built long before the negotiation begins, and rarely explained after it ends.

02 The Twelve Categories

These twelve discounts do not all hit the founder the same way. Some compress price early. Others appear later as deal structure: earnout provisions, indemnity clauses, escrow holdbacks, or a repricing event when diligence surfaces something the initial model did not price. Both reduce the founder's outcome. The distinction matters because they require different preparation and operate on different timelines.

REVENUE QUALITY

Cohort decay pattern. Net revenue retention is a well-understood metric. What is less understood is that buyers do not evaluate it as a number. They evaluate it as a direction. A business reporting one hundred and six percent NRR across all cohorts presents a different asset to a buyer when its most recent customer vintage is tracking at ninety-eight percent. Cohort decay tells a buyer that the conditions producing historical retention are weakening. The discount applied to that signal is not marginal. It is applied to the multiple as a whole, because a deteriorating trend in recent data is the most credible evidence of where the business is going.

Services dependency embedded in software margin. When a software business requires significant professional services to deploy, configure, or retain customers, buyers separate the true software margin from the blended margin the business reports. A company presenting sixty-five percent gross margin that reveals a true software margin of forty-eight percent once professional services costs are correctly classified is a fundamentally different asset. The discount applied is not arithmetic. Buyers do not simply reduce the multiple to reflect lower margin. They reclassify the business, which changes the peer group against which it is valued and the logic of the acquisition itself.

Untested pricing power. The previous issue identified pricing power evidence as a lever buyers underwrite. The shadow process examines whether prices have actually moved, how contracts are structured, whether price increases have historically required material concession to retain customers, and whether implicit or explicit caps are embedded in multi-year agreements. A founder who has never tested pricing power is presenting a hypothesis. Buyers value hypotheses at a discount to demonstrated evidence.

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COMMERCIAL TRANSFERABILITY

Founder-as-product risk. This is the most consistent source of silent discount in Australian mid-market software transactions. A buyer examining the sales history, key customer relationships, product direction decisions, and internal escalation patterns will form an independent view of whether the business is portable without the founder, or whether the founder is not merely leading the business but constituting it. No management presentation corrects for this, because the evidence that would correct for it cannot be produced in one. The record of genuine organisational independence takes twenty-four months to build.

Go-to-market channel concentration. A business that has grown primarily through a single channel: a referral network, a partner relationship, a marketplace dependency, or an outbound team built around one or two high performers, presents a concentration risk that does not appear in the ARR or the customer count. The buyer's question is not whether the channel is working. It is whether the channel is transferable, contractually protected, and independent of the founder's personal relationships.

Second-tier leadership depth. Issue 02 identified leadership independence as a lever. The shadow process examines a more specific question: what exists at the level below the senior leadership team? A business where the three most senior leaders can operate independently, but whose second tier consists of individuals

who joined in the last eighteen months, have not navigated a commercial downturn, and carry institutional knowledge that lives in undocumented practice rather than systematic process, presents fragile organisational architecture. Buyers model attrition assumptions for the post-acquisition period. Those assumptions become more conservative when the depth beneath the leadership layer is thin.

LEGAL AND STRUCTURAL PORTABILITY

Co-created IP ambiguity. Software built with or for customers creates a category of IP ownership question that many founders have not resolved. Where custom development has been performed under client contract, where configuration or integration work sits in a legal grey area between the vendor's IP and the client's environment, or where former employees retain rights that were never formally assigned, buyers face a transferability risk they will price explicitly. Legal teams know what it costs to resolve these questions post-acquisition. That cost is applied to the offer, or structured as an indemnity provision, before any conversation with the founder begins.

Technical debt narrative. Strategic acquirers who intend to integrate the acquired product price the cost and timeline of that integration from the first technical review. A business that cannot present a coherent account of its architectural decisions, the tradeoffs made under resource constraints, and a credible roadmap for addressing them is asking the buyer to model integration risk without the information required to do so. They will model it conservatively. What surfaces during technical diligence either confirms that model or reprices it.

Regulatory and compliance exposure. For Australian software businesses with international customers or cross-border data obligations, unresolved gaps in data residency, privacy regulation, or industry-specific certification represent a category of post-acquisition liability that buyers identify and price. Unlike most categories above, this one is capable of producing binary outcomes. Undisclosed compliance exposure encountered during diligence does not produce a quiet discount. It produces a process exit condition, a fundamental repricing event, or a set of indemnity requirements that restructure the deal.

WHERE THE EVIDENCE BREAKS

Cohort visibility gaps. Data integrity was identified in Issue 02 as a lever buyers evaluate. The shadow process prices not just whether the data exists but whether it can be presented in the form buyers need to underwrite. A company that can produce ARR figures but cannot present customer-level cohort analysis with full attribution, or that has definitional inconsistencies in how churn is calculated, is presenting a data posture that increases the buyer's risk model rather than reducing it. The absence of evidence is itself evidence, and it is priced accordingly.

Contract term erosion. Across a customer base accumulated over several years, patterns emerge in commercial terms that are invisible in any individual agreement but visible at the portfolio level. Contracts individually negotiated over time, with escalating carve-outs, non-standard termination rights, or SLA structures that shift risk progressively toward the vendor, create an aggregate exposure that buyers examine at the level of individual terms, not headline metrics. Software Equity Group's analysis of software M&A transactions identifies contract structure and customer concentration as among the primary diligence concerns that inform initial offer positioning, with many institutional buyers becoming uncomfortable once any single customer approaches the 15 to 20 percent range, and the strongest assets typically sitting below 10 percent (Software Equity Group, 2025 Annual SaaS Report).

Category encroachment risk. This is the category most absent from founder preparation conversations in 2024, and the one receiving concentrated attention from acquirers in 2025 and 2026. A business operating in a workflow category where AI-native tools are narrowing the functional gap between the incumbent and the alternative is carrying a risk that a buyer's deal team will price before the founder has named it. EY's recent analysis of software M&A activity identifies AI readiness, architectural scalability, and the defensibility of a business's category position against AI-enabled competition as central technology diligence vectors. Buyers are already assigning valuation uplift to businesses that can demonstrate material AI integration, not surface-level feature adoption. A business that cannot make that case in 2026 is not necessarily unmarketable. But the discount applied to the uncertainty is measurable.

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03 What This Means for the Founder in the Room

The practical question is not whether your business is good. In this part of the Australian market, the categories that most often surface as the hardest-priced are founder-as-product risk, services dependency hidden inside software economics, customer or contract concentration, and evidence gaps in revenue quality. It is which of these twelve discounts a buyer would apply today, and whether you still have time to change the evidence before a process begins.

The categories in the first two groups (Revenue Quality and Commercial Transferability) primarily shape the multiple in the initial offer. These are the discounts that produce a headline number lower than expected. What the founder often cannot do, at six months from a process, is correct them. Cohort decay requires a change in customer success investment and then two or more years of subsequent data for a buyer to read that change as structural. Founder-as-product risk requires a genuine transfer of relationships and decision rights that cannot be compressed into a transition plan.

The categories in the second two groups appear later, as deal structure. A founder who enters diligence with unresolved IP ambiguity, a compliance gap, or cohort data she cannot present at the vintage level does not typically receive a revised offer with a clear explanation. She receives an earnout provision, an escrow holdback, or a retrade, a repricing event framed as a discovery rather than a negotiation. By that point, the leverage she believed she had at the term sheet stage is no longer available.

This is the moment many founders experience as betrayal. In reality, it is usually not betrayal. It is underwriting arriving late.

At twenty-four months, most of these categories are still addressable, but the window is not static. Every quarter spent not examining them is a quarter that reduces the evidence a buyer can verify. Which is why the real advantage of twenty-four months is not more time to negotiate. It is more time to change what the buyer is underwriting. Contract term erosion can be corrected through a systematic renewal programme that introduces standardised terms as agreements come due. Co-created IP can be clarified through a programme of legal remediation that, begun early, is a project with a defined budget and a timeline. Begun at six months, it becomes a liability with neither.

> Founders who achieve the best outcomes are rarely the ones who solved every category. They are the ones who identified the three or four discounts a buyer would price hardest, early enough to remove them.

Next issue: *the model strategic buyers are actually building when they evaluate your business, and why founders almost never see it clearly from inside the company.*

Cube Capital advises founders and boards of Australian software and technology companies on exit preparation and cross-border M&A transactions. The firm works exclusively on the sell side, retained by founders who want an independent view of what their business is worth and what it would take to make it worth more.

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