

Arc Two: The Other Side of the Table

The Number That Decides Your Multiple

Thesis: A founder builds a valuation case from the top down: revenue, growth rate, market size, competitive position. A buyer arrives at the same conversation with a multiple range already fixed. That range was not set by reading the deck. It was set by reading one number the founder rarely treats as primary: the number that tells a buyer whether the revenue compounds or whether it has to be replaced. Two businesses can report the same ARR on the same day. The buyer, reading one number before the meeting begins, already knows which.

01 One Sentence

The term sheet arrived in the late afternoon.

She had been through the number a dozen times. Twelve million in ARR. Twenty-three percent growth year on year. A gross margin above eighty percent. She had checked her figures against publicly disclosed transactions. She had read the analyst reports on comparable multiples in her category. The range her advisor had indicated was between six and nine times ARR, and she had spent enough time with the analysis to know that her business sat in the upper half of it.

The multiple in the letter was five point eight.

There was one paragraph of explanation. She read it twice. Her net revenue retention was eighty-seven percent. That was the sentence. One number, attached to one metric, with no further elaboration. As though it explained everything.

It did.

02 The Treadmill and the Compounding Base

Place two software companies side by side on the same date.

Both report twelve million in annual recurring revenue. Both grew at twenty percent in the prior year. Both have gross margins above seventy-five percent. Both have passed the revenue reconstruction described in Issue 06. Both have customer contracts with standard renewal terms. Both have cleared the IP audit. Both, by every measure the founders have been tracking, are healthy.

A buyer prices them differently.

The first has net revenue retention of one hundred and fourteen percent. Her existing customers, in aggregate, spend more at the end of each year than they did at the beginning. She loses some accounts. The ones she keeps expand. The base, without a single new customer acquired, grows by fourteen percent annually. Her ARR is not just recurring. It is compounding. Each quarter, the existing cohort is worth more than it was the quarter before. The sales team is not maintaining the base. The base is growing beneath them.

The second has net revenue retention of eighty-seven percent. Her existing customers spend less. She retains the majority of them. The ones that stay are largely flat. The base, without new customer acquisition, shrinks by thirteen percent each year. New revenue does not grow the business. It replaces what the business loses. She reports twenty percent growth. What she does not report is that a portion of that growth was spent recovering ground. Some of her sales effort was not building forward. It was running to stay level.

Twelve million in ARR can mean a compounding base. It can also mean a twelve-million-dollar treadmill.

These two businesses have the same number. A buyer reads them as different things.

FOUNDER THESIS

03 The Range Before the Room

Buyers do not arrive at a management presentation and negotiate a multiple from scratch. They arrive with a range already established, built from having applied the same framework to dozens of comparable businesses. The presentation is an opportunity to confirm or revise that range. It is not the starting point for constructing it.

The primary input to that range is net revenue retention.

Buyers call the adjustment it produces the quality multiple. The principle is mechanical and, once seen, cold: a market multiple applied to recurring software revenue assumes a baseline level of quality. That baseline is a business whose existing base is roughly neutral, where churn and expansion offset each other and new customer growth is genuine forward motion rather than recovery. When NRR exceeds that baseline, the multiple expands. When it falls short, it compresses. And the further it falls, the more the buyer is pricing the cost of the treadmill: the proportion of the sales effort spent not building the business forward but running to maintain it where it is.

A business at ninety-five percent NRR and a business at seventy-eight percent are both below the threshold that marks a compounding base. They are not repriced identically. At ninety-five, the buyer sees a manageable gap, probably addressable in one or two account cycles if the underlying drivers are understood. At seventy-eight, the buyer is looking at twenty-two percent annual base erosion. That erosion is not a negotiating variable. It is a structural operating cost embedded in the business model until something fundamental changes.

Most founders understand that NRR matters. Fewer understand that it is the primary driver of the multiple range before growth rate, market position, management quality, or product differentiation is considered. A business with NRR below one hundred arrives at that conversation having already conceded ground before anyone has said a word about price.

The founder who walks in without knowing this has not been given the framework the buyer is already using. She is presenting strengths. The buyer is pricing fundamentals.

04 Two Founders, One Room

A founder experiences ARR as a number. A buyer reads it as a direction.

One business grows from its base. The other rents growth by replacing what it loses. The multiple, set before either founder walks in, reflects which business is which.

05 Before the Letter

Net revenue retention is not a number that can be moved between signing an advisory engagement and distributing an information memorandum. It is the accumulated output of decisions made at the account level over several years: how pricing is structured, whether expansion pathways exist and are used, how customer success is resourced relative to the revenue it manages, and whether churn is addressed account by account before it becomes a cohort-level trend.

A business that arrives at a process with NRR of eighty-seven percent did not arrive there quickly. It will not leave quickly.

The founder who identifies the gap twenty-four months before a process begins has time that the problem actually requires. The customer base can be analysed account by account for the drivers of churn and contraction. Pricing architecture can be reviewed. Expansion motions can be designed and implemented for accounts that have been flat for several cycles. A credible improvement from eighty-seven to ninety-six percent, held across three or four reporting periods, does not simply change the number. It changes the range in which the multiple conversation begins.

The founder who reads about it in a term sheet letter is not in a position to change it. She is being shown the conclusion of an analysis that was completed before anyone arrived.

The multiple was built from one number, before the presentation. The presentation can confirm the range. It rarely rebuilds it.

FOUNDER THESIS

Issue 10 addresses the next dimension: the risk the founder herself represents. Not whether she is capable. Whether the business she has built can operate without her before the first day of new ownership. The question buyers ask quietly, and price carefully, about every business where the founder is the primary commercial relationship, the primary product decision, and the primary reason most of the team showed up.



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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Founder Thesis began with Arc One, *The Prepared Founder Premium* (Issues 01–05).

The Other Side of the Table is Arc Two.

Issue 06 *The Revenue Your Buyer Won't Pay For*

Issue 07 *Your Customers Don't Belong to You*

Issue 08 *Who Actually Owns Your Software?*

Issue 09 *The Number That Decides Your Multiple*

Issue 10 *The Risk You Are*

Issue 11 *You're Not Selling History*

Issue 12 *Technical Debt Is Financial Debt*

Issue 13 *The Deal That Falls Over on the Seller's Side*

Issue 14 *The Prepared Business Premium*