TECH SECTOR OUTLOOK

FOCUS ON RECOVERY PLAYS

BY RICHARD JEANS
SEPTEMBER 2026

Table of contents

Executive summary

Important notice to readers

This report is provided for informational purposes only and should not be interpreted as providing investment advice nor making recommendations to readers.

Plenty of reasons to be optimistic

UK tech stocks continue to find support at around COVID-19 pandemic-level lows, following the ruthless five-year bear market. Indeed, large cap software & services stocks have rebounded by ca.40% over the past five months, while tech hardware remains in focus following the global semi-conductor boom.

While the advancement of large language models (LLMs), combined with massive data centre investment, generated fears of reduced barriers to entry across the software industry, the reality is more complicated, as LLM tokens add a new cost line, and AI advancements add an entirely new level of complexity to business.

Meanwhile, our preferred investment strategy is to focus on potential recovery stocks with attractive valuations while staying clear of hyped-up stocks.

Trading news remains positive

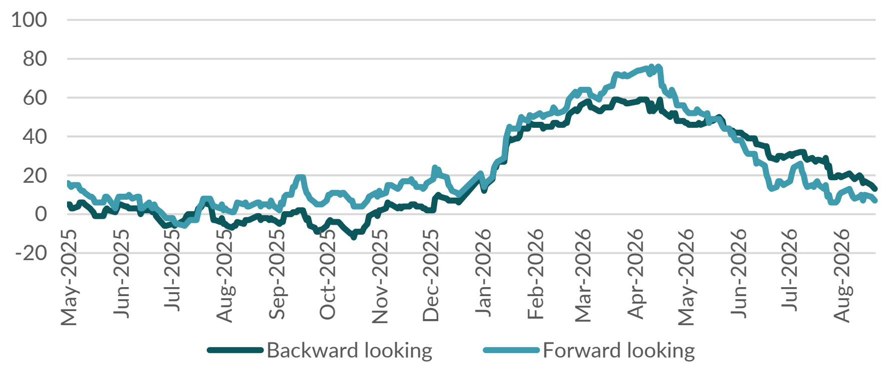
Trading updates continue to be positive, albeit at significantly lower levels than we saw in January through to April this year. This is in spite of the ongoing challenging economic and geopolitical backdrop. Going forward, the question is: can the market generate a similar typical strong first quarter as we move into 2027?

Positive news flow again

We continue to monitor trading updates and earnings announcements of UK tech-related stocks of all sizes, the vast majority of which are small caps. For the purpose of this analysis, our universe is broadly defined and includes IP-driven business across a range of sectors (excluding drug discovery). We monitored 43 companies' statements over August, and – based on commentary (including profit beats/misses, as well as new business wins and outlook statements) – we estimate that ca.40% of these announcements resulted in improvements to the outlook for the individual businesses, compared with 26% that saw decreases.

We quantify these data, as shown in the graph below. On a trading or results announcement, we allocate a +1 for a beat and a -1 for a miss, with a similar process for the perceived outlook. The numbers are aggregated on a quarterly rolling basis, since many companies release trading news each quarter.

Technology-related companies' sentiment indicators



Source: Hardman & Co Research

AI developments

While the advancement of LLMs, combined with massive data centre investment, generated fears of reduced barriers to entry in the software industry, and the subsequent “SaaSpocalyse” sell-off in February, the reality is proving far more complicated. LLM tokens add a new cost line while AI advances effectively have added an entirely new level of complexity to businesses since it increases the number of things that management has to control. There is a plethora of models to choose from, ranging from open source to frontier models, with new models popping up and pricing always evolving. This means corporate governance becomes more of an issue as businesses need to have the appropriate systems and controls in place.

Trading news flow has been healthy

As discussed on page 3, recent trading news has remained generally positive. Recent notable outlook improvements, on our assessments, came from Kainos, Petards, CML Microsystems and Seeing Machines while downgrades were generated by Iforex, Synectics, GB Group and Entain. Kainos is up ca.75% since its low-point in March as the business has shrugged off concerns around a “SaaSpocalyse”.

Balance sheets remain healthy

Of the companies in our software & services indices, two thirds of the constituents have a net cash position. Further, all companies are EBITDA-positive on year 2, where consensus data are available, with just one small cap loss-making in year 1.

Growth drivers remain in place

Digital transformation and AI are still growth drivers

Underlying growth drivers remain in place with the UK software and computer services sector, propelled by a combination of digitalisation, AI adoption, cloud transformation, regulatory pressures and global demand. Industry analysts continue to forecast high single- to low double-digit growth in global IT spending this year.

Shrinking equity supply

We continue to see takeovers while the IPO market remains effectively shut, and secondary fundraisings remain sporadic. Recent software sector takeovers include IDOX, Pinewood and Cordel. In industrial tech, Senior and Gooch & Housego have succumbed to bids, which follows the completion of takeovers of Spectris and Alphawave IP late last year. This shrinking equity supply dynamic continues to remain favourable for the bulls.

Investment conclusion

We look for companies on modest ratings, healthy balance sheets and with strong growth prospects. We prefer to look at EV/EBITDA and the Rule of 40 test (growth plus EBITDA margin is a good overall assessment of the opportunity).

ca.40% of companies in our small cap selection continue to trade at less than 7x Year 2 EBITDA

The small cap space remains modestly valued, with ca.40% of the software and service companies in the selection trading at less than 7x EBITDA in the second year (see table on page 7) while three quarters of the companies have a net cash balance sheet. Seven of the companies – Pinewood (taken over), Cerillion, Seeing Machines, Auction Technology, Intercede, Boku and Dotdigital – pass our simple Rule of 40 test, based on the three years of consensus data.

We look closely at potential recovery situations – stocks on attractive ratings that have been overlooked by the market – while staying clear of hyped-up stocks. TPXimpact is a great example of a recovery success story – management has evolved from an acquisition-driven strategy to focusing on driving organic growth.

AI developments

AI brings new complexities

Indications that the SaaSpocalypse might have been overstated

Soaring investment in AI infrastructure, including data centres, led to a sell-off of Software-as-a-Service companies in February. This sell-off, referred to as the SaaSpocalypse, was due to the concerns that the heavy AI investment would lead to disruptions across the software sector as the AI advancements were making coding so much easier. However, the technology advancements also bring significant new complexities, including far greater volumes of code, as well as a shift to agentic systems. Consequently, security changes fundamentally and data governance becomes much harder.

Meanwhile, the transition of the major LLM vendors – OpenAI, Anthropic and Microsoft – to usage-based revenue models resulted in soaring LLM token spends by corporates. In May, Uber Technologies, the ride booking platform, said that it had spent its entire AI budget in the first four months of the year. This generated speculation that some companies might have spent their entire 2026 AI budget in the first quarter. Consequently, some companies imposed token spending limits on employees, and this also inspired a shift to opensource and cheaper models. The AI inference cost peaked in late May and has broadly halved since then.

This episode highlights the importance of corporate governance. Companies need to determine what systems and controls, such as spending limits, classification systems or model routers, they need to have in place to manage their LLM usage. Interestingly, Stripe acquired OpenRouter in August. OpenRouter provides a common API through which the customer can access hundreds of models and corporate governance tools that include provider restrictions, zero-data-retention routing, price limits and geographic routing.

There are strong indications that the AI revolution has been generating productivity improvements among large caps. Microsoft's employee numbers, including engineers, have been in decline in recent years, while Salesforce's engineers have flatlined and SAP employee numbers have significantly lagged revenue growth. Small cap software companies have also been shedding software engineers, but there is strong demand for engineers with AI skills, and they command markedly higher salaries.

UK SaaS company Pinewood Technologies saw an approach in late January. However, the predator, Apax, stepped aside due to the SaaSpocalypse. A new bidder – Ridgeview – turned up over the summer, once the markets had stabilised and there was greater clarity on the evolving AI backdrop. Pinewood has agreed to Ridgeview's offer of 448p, which is ca.10% below the indicated offer by Apax in January.

Kainos, the UK technology services group, released a strong update in August, upgrading its outlook for FY'27. The group saw momentum across all three of its operating divisions, including its two Workday-focused units. Nasdaq-listed Workday has been in takeover talks with Silver Lake, and this is another indication that the SaaSpocalypse has been overstated. Salesforce shares jumped following its 2Q results in late August, which revealed that its AI products were gaining traction, providing a further indication that the SaaSpocalypse has been overstated.

In May, AIM-listed Cordel agreed to a bid by Vossloh, the German transport-technology group, at a 107% premium, highlighting the extreme undervaluation of some quoted growth companies. The acquisition was completed in August. Cordel is focused on providing AI solutions to the rail industry.

Tech sector performance

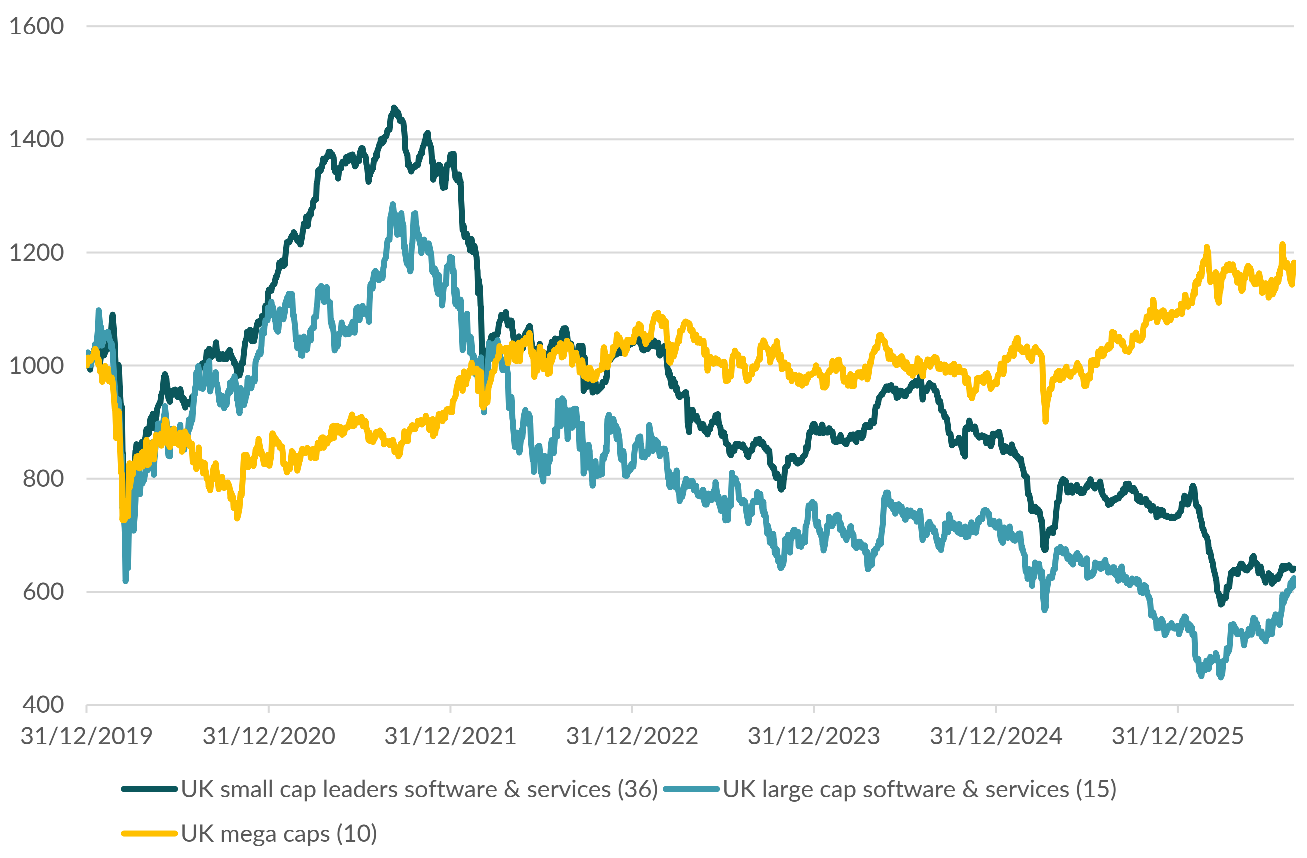
Divergence from blue chip indices in spite of the growth profiles

We follow equal-weighted indices of 15 large cap and 36 small cap UK software services companies and compare these indices with an equal-weighted section of 10 UK mega caps. The latter acts as a useful proxy for the broader weighted index.

Both small and large software & services indices follow a similar pattern. After slumping with the broader markets when COVID-19 hit in early 2020, software and services stocks were swept up as the economy was flooded with liquidity, substantially outperforming the broader markets. Both indices peaked in September 2021 but, subsequently, fell back when inflation hit and rates were tightened.

While large cap software & services stocks have jumped by ca.40% over the past five months, it is a small recovery since the peak in 2021. Technology service companies Computacenter, Softcat, Kainos and Bytes have led the rally and Computacenter has joined the FTSE-100 blue chip index. Our large cap index constituents have changed dramatically over recent years, as many of the major UK software businesses, such as Aveva, Avast, Microfocus and Blue Prism, have been taken over.

Software and services performance against mega caps since before COVID-19



Source: Hardman & Co Research, LSEG data

Small caps remain subdued

Small caps finding support at COVID-19 pandemic lows

The small cap index remains at roughly half its September 2021 peak, and hovering around the pandemic lows, and showing signs of stabilising. In our view, this could provide a reason for more opportunistic investors to consider investments in the sector.

Small cap software and services performance since before COVID-19

Source: Hardman & Co Research, LSEG data

Valuations

Sector retains modest valuation multiples with growth

We have constructed a simple valuation table (see page 11) of 36 small cap software and services companies. Although we monitor the broader technology sector, this analysis focuses on software and services companies to ensure there is comparability, while excluding hardware and other disparate technology-related businesses. For simplicity, we have used the consensus forecast balance sheet position as at the end of the first financial year (mostly 31 December 2026) to estimate the enterprise value.

Large cap software and services

Higher valuations reflect their larger scale and more established business models

UK larger cap software and services companies, on average, have significantly higher ratings than the small caps, with FY3 EV/EBITDA of 8.3x, compared with 6.2x for the small caps. Further, the compound revenue growth and margin expansion are more modest, at 7.2% and 50bp, respectively, over this two-year period.

Software and services valuation table

Name	Price (p)	Est. EV (£m)	EV/sales FY1	EV/sales FY2	EV/sales FY3	EV/EBITDA FY1	EV/EBITDA FY2	EV/EBITDA FY3
Sage	1,098.5	11,314	4.09	3.75	3.45	15.3	13.9	12.4
Computacenter	5,150	4,989	0.44	0.41	0.39	11.6	10.7	10.5
Auto Trader	552.2	4,461	6.87	6.51	6.25	10.3	9.7	9.3
Softcat	2,058	3,902	2.27	2.20	2.01	18.1	17.2	15.6
Rightmove	513.2	3,687	8.10	7.51	6.93	11.7	11.1	10.4
Ocado	237.4	2,797	1.83	1.88	1.75	9.0	9.9	8.4
Kainos	1,237	1,366	2.57	2.34	2.12	16.3	14.5	12.8
Playtech	407.2	1,212	1.69	1.61	1.51	5.4	5.3	4.9
Trustpilot	286	1,083	4.70	4.05	3.50	26.4	19.8	14.5
Mony	209.8	1,054	2.34	2.25	2.18	8.0	7.0	6.7
Gamma	1,102	974	1.47	1.42	1.38	6.9	6.7	6.5
Eurowag	105	882	2.81	2.54	2.32	7.0	6.3	5.7
Baltic Classifieds	208.4	870	10.43	9.38	8.46	13.7	12.4	11.3
Trainline	197.4	867	1.94	1.87	1.81	4.8	4.6	4.5
Bytes	415.4	849	3.54	3.25	2.99	12.5	11.4	10.6
Averages of stocks with 3 years of data			**2.04**	**1.93**	**1.82**	**9.6**	**9.0**	**8.3**
Weighted averages of stocks with 3 years of data			**1.82**	**1.70**	**1.62**	**11.5**	**10.8**	**10.0**

Source: Hardman & Co Research, LSEG data. Priced on the morning of 25 August 2026

Small cap software and services

Sector retains modest valuation multiples with growth

Small caps ratings have fallen substantially since our note in March. Focusing on averages of stocks with three years of data, the EV/revenue is 1.35x in FY1, falling to 1.26x in FY2 and 1.17x in FY3, while EV/EBITDA falls from 8.5x to 6.2x over the same period. This equates to ca.9.4% compound revenue growth over the two-year period and a ca.290bp increase in the average EBITDA margins.

Software and services valuation table

Name	Price (p)	Est. EV (£m)	EV/sales FY1	EV/sales FY2	EV/sales FY3	EV/EBITDA FY1	EV/EBITDA FY2	EV/EBITDA FY3
Auction Technology	441.6	618	3.34	3.17	2.99	9.7	8.7	7.9
RWS	121.5	513	0.72	0.61	0.57	4.7	4.1	3.7
Pinewood	447	490	8.67	5.33	3.75	23.0	15.3	8.3
Alfa Financial Software	167.6	467	3.47	3.22	3.01	10.9	10.0	10.8
Craneware	1280	421	2.76	2.54	2.38	8.7	8.1	7.6
GB Group	155.6	416	1.41	1.34	1.26	6.4	5.6	5.2
NCC	141.8	397	1.35	1.42	1.51	9.0	12.0	13.2
Elixirr	634	361	1.95	1.81	1.69	6.5	6.0	5.6
Seeing Machines	4.75	256	3.53	3.06	2.46	178.8	16.3	8.9
Cerillion	960	255	4.83	4.35	3.99	10.7	9.6	8.8
Advanced ADVT	175	230	4.03	3.89	n/a	14.8	13.9	n/a
Fintel	184	222	2.54	2.44	2.46	7.7	7.1	6.8
Boku	114.5	208	2.01	1.76	1.58	7.2	6.0	5.3
Netcall	118.5	183	3.17	2.72	n/a	15.1	12.3	n/a
Team Internet	44.5	179	0.59	0.56	0.51	5.3	4.8	4.4
Dotdigital	54.7	159	1.73	1.53	1.41	5.4	4.9	4.5
Beeks Financial Cloud	219.5	149	3.70	3.29	n/a	9.6	8.3	n/a
Fonix	174.5	148	1.81	1.69	1.53	9.3	8.6	7.8
Tribal	61.8	135	1.44	1.44	1.42	7.9	8.4	7.9
Eagle Eye	485	133	2.91	2.57	2.28	15.1	12.2	10.2
Activeops	192.5	129	2.67	2.46	2.37	22.3	17.1	15.9
Eleco	126	123	3.07	2.80	n/a	11.5	9.9	n/a
Quartix	225	104	2.55	2.36	n/a	6.9	6.4	n/a
FDM	116	96	0.59	0.53	0.49	5.1	4.1	3.7
Aptitude	217	93	1.28	1.19	n/a	7.7	6.9	n/a
Tracsis	335	92	1.09	1.20	1.12	6.8	5.9	5.2
Accesso	305	90	0.83	0.80	0.76	6.0	5.6	5.2
Redcentric	104	73	0.55	0.53	0.50	4.2	4.0	3.3
Software Circle	15.75	68	n/a	n/a	n/a	n/a	n/a	n/a
Microlise	50	51	0.61	0.58	n/a	4.8	4.3	n/a
Intercede	112.5	51	2.41	2.11	1.87	10.1	8.0	6.3
Bango	63	47	1.12	1.13	n/a	3.2	3.0	n/a
Corero Network Security	7.25	34	1.56	1.38	1.23	13.7	9.7	7.2
Skillcast	44	27	1.58	1.39	n/a	12.3	7.5	n/a
Celebrus	93	10	0.57	0.52	0.49	(16.9)	12.3	7.1
Oxford Metrics	40	10	0.19	0.19	n/a	1.3	1.2	n/a
Averages of stocks with at least 2 yrs' data			**1.20**	**1.13**	**n/a**	**7.2**	**6.1**	**n/a**
Averages of stocks with 3 years of data			**1.35**	**1.26**	**1.17**	**8.5**	**7.2**	**6.2**
Weighted averages of stocks with 3 years of data			**1.70**	**1.56**	**1.47**	**8.3**	**7.4**	**6.7**

Source: Hardman & Co Research, LSEG data. Priced on the morning of 25 August 2026

Conclusion

While AI-disruption fears have abated and larger cap software and services companies have rallied in recent months, small caps remain modestly rated. We continue to suggest that investors should focus on stocks with healthy balance sheets and attractive valuation metrics. Stocks that pass the Rule of 40 test and have strong financial position warrant a more serious consideration.

In summary, we highlight the following points supporting the investment case for UK technology stocks:

- Recent trading news remains positive, albeit at lower levels than earlier this year
- Takeover activity remains brisk across the broader UK market
- Limited equity supply remains supportive
- Software and services sector valuations are attractive
- Software and services sector balance sheets are mostly healthy
- Small cap software and services stocks remain around pandemic lows

About the author

Richard Jeans

Richard Jeans is an equity analyst at Hardman & Co, covering the technology sector.

Richard has worked in the investment research industry and financial media for over 35 years. He has covered small cap technology stocks from across the globe for more than 15 years. He has built up a strong knowledge of the global capital markets, having worked on the capital markets desk at the Financial Times. Prior to that, he worked at an independent equity research company in the early 1990s. Brought up in New Zealand, his first job involved compiling the stock market data for New Zealand's largest newspaper.

Richard joined Hardman & Co in 2023. He is an ASIP, and has been a member of the CFA Institute and its predecessor organisations since 1990.

Disclaimer

Hardman & Co provides professional independent research services and all information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable. However, no guarantee, warranty or representation, express or implied, can be given by Hardman & Co as to the accuracy, adequacy or completeness of the information contained in this research and they are not responsible for any errors or omissions or results obtained from use of such information. Neither Hardman & Co, nor any affiliates, officers, directors or employees accept any liability or responsibility in respect of the information which is subject to change without notice and may only be correct at the stated date of their issue, except in the case of gross negligence, fraud or wilful misconduct. In no event will Hardman & Co, its affiliates or any such parties be liable to you for any direct, special, indirect, consequential, incidental damages or any other damages of any kind even if Hardman & Co has been advised of the possibility thereof.

This research has been prepared purely for information purposes, and nothing in this report should be construed as an offer, or the solicitation of an offer, to buy or sell any security, product, service or investment. The research reflects the objective views of the analyst(s) named on the front page and does not constitute investment advice. However, the companies or legal entities covered in this research may pay us a fixed fee in order for this research to be made available. A full list of companies or legal entities that have paid us for coverage within the past 12 months can be viewed at http://www.hardmanandco.com/legals/research-disclosures. Hardman may provide other investment banking services to the companies or legal entities mentioned in this report.

Hardman & Co has a personal dealing policy which restricts staff and consultants' dealing in shares, bonds or other related instruments of companies or legal entities which pay Hardman & Co for any services, including research. No Hardman & Co staff, consultants or officers are employed or engaged by the companies or legal entities covered by this document in any capacity other than through Hardman & Co.

Hardman & Co does not buy or sell shares, either for their own account or for other parties and neither do they undertake investment business. We may provide investment banking services to corporate clients. Hardman & Co does not make recommendations. Accordingly, they do not publish records of their past recommendations. Where a Fair Value price is given in a research note, such as a DCF or peer comparison, this is the theoretical result of a study of a range of possible outcomes, and not a forecast of a likely share price. Hardman & Co may publish further notes on these securities, companies and legal entities but has no scheduled commitment and may cease to follow these securities, companies and legal entities without notice.

The information provided in this document is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject Hardman & Co or its affiliates to any registration requirement within such jurisdiction or country.

Some or all alternative investments may not be suitable for certain investors. Investments in small and mid-cap corporations and foreign entities are speculative and involve a high degree of risk. An investor could lose all or a substantial amount of his or her investment. Investments may be leveraged and performance may be volatile; they may have high fees and expenses that reduce returns. Securities or legal entities mentioned in this document may not be suitable or appropriate for all investors. Where this document refers to a particular tax treatment, the tax treatment will depend on each investor's particular circumstances and may be subject to future change. Each investor's particular needs, investment objectives and financial situation were not taken into account in the preparation of this document and the material contained herein. Each investor must make his or her own independent decisions and obtain their own independent advice regarding any information, projects, securities, tax treatment or financial instruments mentioned herein. The fact that Hardman & Co has made available through this document various information constitutes neither a recommendation to enter into a particular transaction nor a representation that any financial instrument is suitable or appropriate for you. Each investor should consider whether an investment strategy of the purchase or sale of any product or security is appropriate for them in the light of their investment needs, objectives and financial circumstances.

(Disclaimer Version 9 – Approved July 2025)

Status of Hardman & Co's research under MiFID II

Hardman & Co's research is paid for by the companies, legal entities and issuers about which we write and, as such, falls within the scope of 'acceptable minor non-monetary benefits', as defined in the Markets in Financial Instruments Directive.

The FCA Handbook (COBS 2.3A.19) states: 'An acceptable non-monetary benefit is one which:[...] (5) consists of: [...] (b) written material from a third party that is commissioned and paid for by a corporate issuer or potential issuer to promote a new issuance by the company, or where the third party firm is contractually engaged and paid by the issuer to produce such material on an ongoing basis, provided that the relationship is clearly disclosed in the material and that the material is made available at the same time to any firms wishing to receive it, or to the general public.'

The fact that Hardman & Co is commissioned to write the research is disclosed in the disclaimer, and the research is widely available.

About Hardman & Co

We are a rapidly growing, innovative corporate research & consultancy business, based in London, serving the needs of both public and private companies.

Our expert team of sector analysts and market professionals collectively have over 400 years of experience. This depth of knowledge and a reputation for integrity have built trust with investors. With effective communication and precision distribution, we help companies disseminate their investment message to interested investors, as well as advise them on strategy.

Our smaller, boutique structure allows us to provide first-class customer service and to deliver a wide range of ad-hoc services for multiple clients with different needs.

Front cover image designed by Magnific.

research@hardmanandco.com

9 Bonhill Street
London
EC2A 4DJ

www.hardmanandco.com