Rule of 40: 2026 Benchmark Report

The Rule of 40 has stopped sorting. **28 of 44** listed software companies clear it on Windsor Drake's computation as of 17 August 2026, a **64%** pass rate against the **16%** Bain measured across 124 companies in 2017, with a median score of **43.6**. A test that two thirds of the population passes is no longer a test. It is a floor, and floors do not price assets.

The deeper problem is arithmetic rather than calibration. The rule adds a point of growth to a point of margin and treats them as equals. The market does not. Revenue growth correlates with EV/Revenue at **0.59**; free cash flow margin correlates at **0.08**. On a two-variable fit a point of growth is worth **2.3 times** a point of margin. Two companies can post an identical score and be worth very different amounts, and they routinely are.

The evidence is unambiguous at the top of the range. Among companies scoring 50 to 70, growth-led businesses trade at a median **17.7x** EV/Revenue against **9.1x** for profit-led ones. Same score band, nearly double the multiple. Meanwhile the median constituent runs **25.5%** free cash flow margin against **16.3%** growth, having optimised the half of the equation the market pays least for.

Clearing the threshold also offered no protection when conditions turned. Roughly **$2 trillion** of software market value was erased between October 2025 and February 2026 and median SaaS EV/Revenue fell from **6.2x to 3.3x**. This report sets out what the rule actually measures in 2026, where the multiple genuinely inflects, and what a founder should optimise instead.

How many software companies actually clear the Rule of 40 in 2026?

Every score in this report is computed from reported company financials rather than licensed. Growth is the most recent reported quarter against the same quarter a year earlier, and margin is free cash flow margin on the trailing twelve months. Constituents are named so the calculation can be reproduced or disputed.

Table 1. Rule of 40 Clearance Rates, 2017 to 2026

Measurement	Population	Clearance rate	Source
Bain, 2017	124 companies	16%	Bain & Company
McKinsey, 2011 to 2021	Software universe	16% of the time	McKinsey & Company
Windsor Drake, August 2026	44 listed companies	64%	Windsor Drake computation

Source: Bain & Company; McKinsey & Company; Windsor Drake computation from reported company financials, 17 August 2026.

A fourfold rise in the clearance rate is not evidence that software has become four times better run. It is evidence that the population has reweighted toward margin during a period when capital was expensive, and that the threshold was calibrated for a different cost of capital. The rule now sorts the bottom third of the market from the rest, which is a narrower job than the one it is usually asked to do.

Is growth or margin more valuable inside the score?

This is the question the rule is built to avoid answering, and it is the one that determines the multiple. Growth and free cash flow margin enter the score with equal weight and leave the market with very unequal weight.

Table 2. What the Market Actually Weights, August 2026

Input	Correlation with EV/Revenue	Relative weight
Revenue growth	0.59	2.3x
Free cash flow margin	0.08	1.0x
Rule of 40 score, combined	Weaker than growth alone	Obscures the difference

Source: Windsor Drake computation across the 44-company constituent set, 17 August 2026. Relative weight is from a two-variable fit.

A correlation of 0.08 means free cash flow margin explains almost nothing about where a software company trades on revenue. That is not an argument for unprofitable growth; it is an argument that margin is a hygiene factor and growth is a pricing factor, and that a composite treating them as equals will mislead any founder who optimises against it.

Two identical scores, two different companies

Among constituents scoring 50 to 70, growth-led businesses trade at a median **17.7x** EV/Revenue and profit-led businesses at **9.1x**. The score cannot distinguish them because it was designed not to. A buyer distinguishes them immediately, because durable growth is what agentic substitution most directly threatens and what is hardest to manufacture in a diligence period.

Where does the multiple actually inflect?

Not at 40. The banded data shows the meaningful step change occurring above 50, with the sharpest repricing above 60. A company at 41 and a company at 39 are not on opposite sides of a valuation cliff, whatever the rule implies.

Table 3. EV/Revenue by Rule of 40 Band, August 2026

Rule of 40 score	Median EV/Revenue	Read
Above 60	21.4x	Where the market genuinely repays the score
50 to 60	10.0x	The real inflection point
40 to 50	5.7x	Clearing the threshold, modestly rewarded
30 to 40	4.6x	Near miss, small discount to the band above

Source: Windsor Drake computation from reported company financials and market capitalisation, 17 August 2026.

The gap between the 40 to 50 band and the 50 to 60 band is larger than the gap between the 30 to 40 band and the 40 to 50 band. The threshold that matters commercially sits ten points above the one the industry quotes, and a founder targeting 40 is targeting the wrong number.

Did clearing the Rule of 40 protect valuations in the 2026 repricing?

No. Between October 2025 and February 2026 roughly **$2 trillion** of software market value was erased and the median SaaS EV/Revenue multiple fell from **6.2x to 3.3x**, close to a halving. The repricing was driven by a reassessment of whether seat-based recurring revenue is durable against agentic artificial intelligence, and that question is orthogonal to the score.

Table 4. The 2026 Software Repricing

Measure	Before	After
Median SaaS EV/Revenue	6.2x	3.3x
Software market value	Peak, October 2025	Roughly $2 trillion lower by February 2026
What was repriced	Seat-based recurring revenue	Durability against agentic substitution
Protection offered by clearing 40	None observable	Score did not predict which assets held

Source: Windsor Drake analysis of public market data; company filings. Multiples computed on the same basis before and after.

The lesson is not that operating discipline stopped mattering. It is that a composite score measuring last year's operating performance says nothing about whether next year's revenue survives, and buyers in 2026 are underwriting the second question.

What should founders do now?

Use the rule as a floor and argue the multiple on the components. Three moves follow directly from the data.

First, report growth and margin separately and lead with growth where the business has it, because the market prices growth at 2.3 times the weight it gives margin. A composite score presented without its components invites a buyer to assume the less valuable mix. Second, target 50 rather than 40, since that is where the multiple genuinely inflects, and understand that the distance from 45 to 55 is worth considerably more than the distance from 35 to 45. Third, evidence revenue durability directly, with net revenue retention, documented switching costs and cohort data, because that is what the 2026 repricing tested and the score does not capture it.

A full sale process runs 12 to 18 months, so the operating profile a founder presents at close reflects decisions taken well before preparation began. Margin can be produced inside a year. Durable growth cannot, and it is the half the market pays for.

Key takeaways for founders

Translating the analysis into strategy means concentrating on six areas that consistently move software valuations in the current environment.

1. The rule is a floor, not a differentiator

64% of listed software companies clear it, against 16% when Bain measured in 2017. Clearing 40 no longer distinguishes a business; failing it still flags one.

2. Growth is worth 2.3 times margin

Revenue growth correlates with EV/Revenue at 0.59 and free cash flow margin at 0.08. Optimise and present accordingly, and never let a composite hide which half of the score you actually have.

3. The inflection is at 50, not 40

Median EV/Revenue runs 4.6x below 40, 5.7x from 40 to 50, 10.0x from 50 to 60 and 21.4x above 60. Ten points above the industry threshold is where the repricing happens.

4. Same score does not mean same value

In the 50 to 70 band, growth-led companies trade at 17.7x against 9.1x for profit-led ones. Two identical scores, nearly double the multiple.

5. The median company optimised the wrong half

The median constituent runs 25.5% free cash flow margin against 16.3% growth. Margin already taken cannot be taken again, and it is the input the market rewards least.

6. Durability is what gets underwritten now

Clearing 40 offered no protection when roughly $2 trillion of software value was erased and median multiples fell from 6.2x to 3.3x. Evidence net revenue retention, switching costs and cohort behaviour, because that is the question a buyer is actually asking.

- Bain & Company, Rule of 40 clearance analysis and Global Private Equity Report 2026
- McKinsey & Company, software performance and the Rule of 40, 2011 to 2021
- McKinsey & Company, 2025 Technology Outlook
- Boston Consulting Group, The AI-First SaaS Company: Rethinking the Playbook
- Goldman Sachs, 2026 Global M&A Outlook and Technology in 2026
- Morgan Stanley Research, AI market trends 2026 and software sector notes
- S&P Global Market Intelligence, software sector valuation data
- PitchBook, enterprise software public comparable data
- EY, Global IPO Trends and Private Equity Pulse
- Federal Reserve, FOMC statement and Summary of Economic Projections
- U.S. Securities and Exchange Commission, company filings for all screened constituents

Methodology Note

Framework. The Growth Point Premium is a Windsor Drake framework. It decomposes the Rule of 40 into its two inputs and prices them separately against observed market data rather than accepting the equal weighting the rule imposes. The finding that a point of growth is worth 2.3 times a point of margin is the firm's own computation and is published so it can be argued with.

Source standard. Inputs are restricted to top-tier institutions: bulge-bracket banks, the major consultancies, elite data houses, and primary regulatory and filing sources. Boutique and market-report vendors are excluded, as are rival advisory firms.

How the scores were computed. Every Rule of 40 score is Windsor Drake's own computation from reported company financials. Growth is the most recent reported quarter against the same quarter a year earlier. Margin is free cash flow margin on the trailing twelve months. Market capitalisation is as of 17 August 2026 and revenue is from each company's most recently reported fiscal quarter. No score in this report is licensed from a data vendor.

Correlation and weighting. Correlations are computed across the 44-company constituent set on the same date. The 2.3x relative weight comes from a two-variable fit of growth and free cash flow margin against EV/Revenue, and is presented as a house estimate rather than a precise coefficient.

Synthesis and attribution. Figures labelled as firm analysis or house estimate are Windsor Drake's own synthesis of the cited institutional data, presented as a house view rather than third-party consensus. Where current-quarter data was not yet published, the most recent available data is used.