

TXT e-solutions

Acquiring Italian software testing business

Q1 results, acquisition

Software & comp services

15 May 2019

Price €8.57
Market cap €101m

Net cash (€m) at end Q119	61.1
Shares in issue	11.7m
Free float	45%
Code	TXT
Primary exchange	Borsa Italiana (STAR)
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(7.3)	(11.6)	(30.6)
Rel (local)	(2.8)	(15.4)	(19.2)
52-week high/low	€12.32	€7.70	

Business description

TXT e-solutions provides IT, consulting and R&D services to aerospace, aviation, automotive, banking and finance customers.

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H119 results	1 August 2019
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With the acquisition of Assioma, TXT continues to deploy its substantial cash pile. The deal doubles the size of its financial institution-focused software testing business and is earnings accretive. The company announced strong Q119 revenue and net income growth, with a particularly good performance from the Aerospace, Aviation & Automotive business. We have revised our forecasts to reflect the acquisition and Q1 results, with EPS upgrades of 31% and 22% in FY19 and FY20 respectively.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/17	35.9	3.0	0.19	1.00	46.1	11.7
12/18	40.0	1.5	0.10	0.50	83.4	5.8
12/19e	54.3	5.2	0.31	0.13	28.0	1.5
12/20e	61.2	5.9	0.34	0.15	24.9	1.8

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Doubling the size of the Banking & Finance division

On 1 May, TXT acquired Assioma, an Italian software testing business focused on the Italian banking sector. On a pro forma basis, this doubles the size of the Banking & Finance division and increases its profitability. The deal will cost up to €9.3m, with €4.3m already paid out in cash, and €0.3m in cash and €2.3m worth of shares in escrow until the end of May. Up to €2.4m is payable for earnouts over the medium term, treated as long-term debt in our forecasts.

Impressive organic growth in Q119

TXT reported Q119 revenue growth of 26.5% y-o-y, and 17.3% organic growth. The Aerospace, Aviation & Automotive (AAA) division was the biggest contributor to organic growth, up 20% y-o-y, with Banking & Finance up 6.6% on an organic basis. The cost base increased at a slightly faster rate than revenues (mainly due to a 63% increase in R&D spend), resulting in normalised EBIT growth of 13.4% y-o-y. Marking to market the €100m invested in multi-segment insurance funds resulted in financial income of €1.3m in Q119, which was the main factor in the 163% increase in net income y-o-y. We have revised our forecasts to reflect Q1 results and the Assioma acquisition, resulting in upgrades to normalised EPS of 31% in FY19 and 22% in FY20. Management confirmed that it continues to seek appropriately priced acquisitions in both divisions.

Valuation: Accretive acquisitions to drive upside

TXT is trading on EV multiples that are at a c 30% discount to peers – by FY20 EBITDA margins are forecast to be broadly in line with peers, although EBIT margins are lower. As the company still has a large proportion of the cash from the sale of TXT Retail (we estimate €50m in net cash by the end of FY19), its P/E multiples are inflated versus peers. We expect this premium to reduce as the company makes earnings-enhancing acquisitions.

Assioma doubles size of Banking & Finance business

TXT has acquired Assioma, an Italian software testing business, with a completion date of 30 April. Assioma will be consolidated from 1 May.

Deal to cost up to €9.3m

TXT has paid initial cash consideration of €4.3m. It has also put €0.3m cash and treasury shares worth €2.3m in escrow (due for release by end May), for a total initial consideration of €6.9m. The shares are being issued at an agreed value of €8.982 per share, ie 253,846 shares. Contingent consideration of up to €2.4m is payable in two tranches based on the achievement of specific operational goals in the medium term.

Background on Assioma

Assioma was founded 30 years ago by current CEO Giovanni Daniele De Stradis. The business currently has 150 employees based in offices in Bari, Milan and Turin. Customers include banks such as Intesa San Paolo, Unicredit Leasing, UBI, ING Direct, Widiba, BPM Group, Allianz and AXA. In 2018, the Assioma group generated revenues of €9.4m, EBITDA of €1.3m (13.9% margin) and net income of €0.9m.

Integration plans

Assioma will continue to trade under its own name and be run by Mr De Stradis. Over time, he will develop integration opportunities with TXT's Banking & Finance division, which also provides software testing services into Italian financial institutions.

Review of Q119 results

Exhibit 1: Quarterly results highlights			
€m	Q119a	Q118a	y-o-y
Revenues	11.9	9.4	26.5%
Licenses & maintenance	1.5	1.1	31.8%
Services	10.4	8.3	25.7%
Gross margin	43.9%	45.1%	-1.2%
EBITDA	1.3	1.2	9.2%
EBITDA margin	10.9%	12.6%	-1.7%
Normalised EBIT	1.0	0.8	13.4%
Normalised EBIT margin	8.1%	9.0%	-0.9%
Reported net income	1.4	0.5	162.9%
Net cash	61.1	87.9	-30.5%

Source: TXT e-solutions

TXT reported 26.5% y-o-y growth in group revenues in Q119. Stripping out the €0.9m contributed by Cheleo (acquired in Q318), the business grew 17.3% y-o-y. Software licenses, subscriptions and maintenance revenues totalled €1.5m, up 31.8% y-o-y and 13.0% on an organic basis. Services revenues totalled €10.4m, up 25.7% y-o-y and 17.9% on an organic basis. On a divisional basis, Aerospace, Aviation & Automotive grew 20.3% y-o-y (all organic) and Banking & Finance grew 49.2% (6.6% organic). Total operating costs before depreciation and amortisation increased 28.5% y-o-y, with R&D seeing the largest increase (+63% y-o-y). This resulted in EBITDA increasing at a slower rate of 9.2% y-o-y and the margin falling from 12.6% to 10.9%. TXT reported financial income of €1.278m (Q118: €17k) as the investment in multi-segment insurance funds was revalued upward during the quarter. This resulted in a net income increase of 162.9% y-o-y.

Changes to forecasts

Management expects an acceleration in revenue growth in Q219, from organic revenues and the Cheleo and Assioma acquisitions. EBITA is expected to be substantially higher than in Q218.

We have revised our underlying forecasts to reflect the revenues reported in Q119 (slightly reducing software revenues but increasing services revenues) and to reflect a higher ongoing level of R&D. Within financial income, we have also factored in a €1m upward revaluation of the multi-segment insurance fund investments for FY19. The company had previously noted that these suffered a downward revaluation of c €1m in FY18, but had nearly recovered the whole amount in Q119.

We have factored in the Assioma acquisition from 1 May 2019. As TXT expects to record the earnouts as long-term debt, we have increased our long-term debt forecasts accordingly. Based on our forecasts for FY20, the acquisition doubles the size of the Banking & Finance business and results in margin expansion on a divisional and group basis. We forecast that TXT will have net cash of €50m by the end of FY19, providing a substantial level of funding for further acquisitions in either the Banking & Finance or Aerospace, Aviation & Automotive divisions.

Exhibit 2: Changes to forecasts								
	FY19e old	FY19e new	Change	y-o-y	FY20e old	FY20e new	Change	y-o-y
Revenues (€m)	46.0	54.3	18.0%	35.8%	49.5	61.2	23.6%	12.8%
Gross margin	45.2%	42.8%	(2.4%)	(1.4%)	45.2%	42.2%	(3.0%)	(0.6%)
Gross profit (€m)	20.8	23.2	11.7%	31.5%	22.4	25.8	15.3%	11.2%
EBITDA (€m)	5.1	5.5	7.3%	33.1%	5.9	7.3	23.8%	33.2%
EBITDA margin	11.1%	10.1%	(1.0%)	(0.2%)	11.8%	11.9%	0.0%	1.8%
Normalised EBIT (€m)	3.5	3.9	12.2%	41.7%	4.3	5.6	32.1%	44.4%
Normalised EBIT margin	7.6%	7.2%	(0.4%)	0.3%	8.6%	9.2%	0.6%	2.0%
Normalised net income (€m)	2.7	3.6	32.2%	198.7%	3.3	4.1	23.9%	13.3%
Normalised EPS (€)	0.23	0.31	31.1%	198.0%	0.28	0.34	22.1%	12.5%
Reported basic EPS (€)	0.17	0.25	42.0%	412.9%	0.22	0.29	28.3%	15.6%
Net cash (€m)	57.7	50.1	(13.2%)	(17.0%)	60.2	53.2	(11.6%)	6.2%
Dividend (€)	0.13	0.13	0.0%	(74.0%)	0.15	0.15	0.0%	15.4%

Source: Edison Investment Research

Exhibit 3: Financial summary

	€'000s	2014	2015	2016	2017	2018	2019e	2020e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		54,410	61,540	33,060	35,852	39,957	54,260	61,202
Cost of sales		(26,455)	(29,189)	(18,954)	(20,224)	(22,289)	(31,035)	(35,384)
Gross profit		27,955	32,351	14,106	15,628	17,668	23,225	25,818
EBITDA		5,324	6,659	4,260	3,536	4,098	5,453	7,262
Operating Profit (before amort and except)		4,284	5,820	3,954	3,180	2,755	3,904	5,638
Amortisation of acquired intangibles		(285)	(285)	(264)	(439)	(610)	(960)	(960)
Exceptionals and other income		1,468	0	(557)	0	(300)	0	0
Other income		0	(740)	0	(69)	0	0	0
Operating Profit		5,467	4,795	3,133	2,672	1,845	2,944	4,678
Net Interest		(249)	(151)	48	(208)	(1,284)	1,300	300
Profit Before Tax (norm)		4,035	5,669	4,002	2,972	1,471	5,204	5,938
Profit Before Tax (FRS 3)		5,218	4,644	3,181	2,464	561	4,244	4,978
Tax		(1,046)	(762)	(661)	(710)	4	(1,188)	(1,394)
Profit After Tax (norm)		3,226	4,739	3,170	2,170	1,204	3,747	4,275
Profit After Tax (FRS 3)		4,172	3,882	2,520	1,754	565	3,056	3,584
Average Number of Shares Outstanding (m)		11.5	11.7	11.7	11.7	11.7	11.7	11.8
EPS - normalised (€)		0.281	0.406	0.271	0.186	0.103	0.306	0.345
EPS - normalised fully diluted (€)		0.276	0.403	0.271	0.186	0.103	0.306	0.345
EPS - (IFRS) (€)		0.364	0.333	0.475	5.874	0.048	0.248	0.286
Dividend per share (€)		0.23	0.25	0.30	1.00	0.50	0.13	0.15
Gross margin (%)		51.4	52.6	42.7	43.6	44.2	42.8	42.2
EBITDA Margin (%)		9.8	10.8	12.9	9.9	10.3	10.1	11.9
Operating Margin (before GW and except) (%)		7.9	9.5	12.0	8.9	6.9	7.2	9.2
BALANCE SHEET								
Fixed Assets		18,019	18,132	25,428	8,860	22,942	30,323	28,179
Intangible Assets		15,078	14,692	21,296	7,332	17,751	25,963	24,975
Tangible Assets		1,249	1,361	1,598	793	3,680	2,849	1,693
Other		1,692	2,079	2,534	735	1,511	1,511	1,511
Current Assets		34,892	38,946	37,085	109,426	134,674	119,777	117,633
Stocks		1,820	2,075	3,146	2,528	3,141	3,441	3,741
Debtors		20,768	27,791	26,369	17,215	16,992	23,075	26,027
Cash		12,304	9,080	7,570	89,683	114,541	93,261	87,865
Other		0	0	0	0	0	0	0
Current Liabilities		(17,451)	(18,349)	(21,051)	(13,612)	(30,086)	(29,648)	(31,814)
Creditors		(15,297)	(17,528)	(20,243)	(12,937)	(12,782)	(17,244)	(19,410)
Short term borrowings		(2,154)	(821)	(808)	(675)	(17,304)	(12,404)	(12,404)
Long Term Liabilities		(6,491)	(5,105)	(7,180)	(4,781)	(41,184)	(35,084)	(26,584)
Long term borrowings		(1,685)	0	(1,391)	(1,688)	(36,882)	(30,782)	(22,282)
Other long term liabilities		(4,806)	(5,105)	(5,789)	(3,093)	(4,302)	(4,302)	(4,302)
Net Assets		28,969	33,624	34,282	99,893	86,346	85,368	87,414
CASH FLOW								
Operating Cash Flow		5,404	2,412	10,676	119	2,039	3,533	6,175
Net Interest		(249)	(151)	105	(208)	(69)	1,300	300
Tax		(1,344)	(1,461)	(2,022)	379	(624)	(1,188)	(1,394)
Capex		(615)	(763)	(738)	(661)	(526)	(440)	(440)
Acquisitions/disposals		0	0	(5,403)	82,250	1,314	(9,400)	0
Financing		(597)	2,215	(828)	(6)	(7,227)	(674)	0
Dividends		(2,615)	(2,678)	(2,931)	(3,496)	(11,710)	(5,913)	(1,537)
Net Cash Flow		(16)	(426)	(1,141)	78,377	(16,803)	(12,783)	3,104
Opening net debt/(cash)		(8,575)	(8,465)	(8,259)	(5,371)	(87,320)	(60,358)	(50,075)
HP finance leases initiated		0	0	0	0	(2,788)	0	0
Other		(94)	220	(1,747)	3,572	(7,371)	2,500	0
Closing net debt/(cash)		(8,465)	(8,259)	(5,371)	(87,320)	(60,358)	(50,075)	(53,179)

Source: TXT e-solutions, Edison Investment Research

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