

artec technologies

Technology

21 June 2019

Positioning for growth

artec recorded a strong 2018, with revenues doubling to €2.9m and the group returning to a small profit. It received a number of important reference orders over the year, which adds impetus to marketing and boosts the potential for future growth. In addition, early this year a major US competitor, Verizon Digital Media Services (VDMS), unexpectedly said it was exiting the market. This provides additional possibilities for artec if VDMS's European customers (Volicon Observer product) are interested in an alternative supplier. If management can sustain the momentum, we believe there is significant upside in the shares.

FY18: Underlying EBIT margin was 10%

FY18 revenue doubled to €2.9m and artec returned to a small operating profit (EBIT) of €33k from a €776k loss in FY17. Management says that excluding one-off costs, the EBIT margin was c 10%. Last year, artec undertook a 10% capital increase, raising c €0.9m to provide working capital to deliver on major contract wins. The group ended the year with a modest cash position of €46k, it has no financial liabilities and its equity ratio increased over the period from 86% to 93%. New business momentum continues, with the group having attained five of the 14 German state media offices as customers and it has acquired an ex-Volicon customer in France and expanded its offering with a customer in Qatar.

Evolving strategy

In FY18 management outlined a new strategy focused on targeting state agencies and public authorities in the DACH (German-speaking) countries, while also offering scalable cloud/SaaS offerings to the media and broadcast sector. artec seeks to build its sales through a partnering approach. With regard to technology, it offers a buy, build, partner approach – as well as developing some of its own IP, it will partner other software vendors to take advantage of established solutions that can be bolted on to its MULTIEYE and XENTAURIX platforms and will consider acquiring small vendors with innovative solutions. Management is now deciding its plans to target the Volicon customer base, which would involve a fresh round of investment including expansion of headcount.

Valuation: An option on a massive opportunity

artec's target markets are large and we see its modest €11.7m market capitalisation as an option on management's ability to leverage the company's significant success stories/case studies into a more scalable and profitable business model.

Historical financials

Year end	Revenue (€m)	EBITDA (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/15	3.5	1.0	0.22	0.0	20.4	N/A
12/16	2.5	(0.1)	(0.13)	0.0	N/A	N/A
12/17	1.5	(0.4)	(0.34)	0.0	N/A	N/A
12/18	2.9	0.4	0.01	0.0	N/A	N/A

Source: artec

Price €4.49

Market cap €12m

Share price graph



Share details

Code	A6T
Listing	Deutsche Börse Scale
Shares in issue	2.6m
Last reported net cash at 31 Dec 2018	€46k

Business description

artec technologies develops and produces software and systems solutions for the transmission, recording and analysis of video, audio and metadata in networks or on the internet.

Bull

- Strong customer list and some excellent case studies.
- Heavily invested in IP, through many years of experience, supported by a German patent.
- Shifting to a more scalable cloud/SaaS business model.

Bear

- Small scale and limited staff resources for projects.
- Small balance sheet position, with limited cash resources.
- Volatile trading record.

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Technology for video security and media analysis

artec technologies is a specialist in recording and storing audiovisual information. The company operates in two market segments with two key products, which are based around the same core technology – video security (MULTIEYE) and media analysis systems (XENTAURIX). Approximately 60% of the business is in security with the balance in media and broadcast. However, in our view the media and broadcast business has greater growth prospects and we would expect these numbers to switch over the medium term.

artec integrates third-party technologies into its platforms and the functionality includes number-plate recognition, facial recognition, sentiment analysis, ratings analysis and video fingerprinting. The platform also incorporates artificial intelligence (AI) from Finnish AI specialist Valossa and artec's XENTAURIX AI platform was demonstrated at the IBC trade show in Amsterdam. artec constantly seeks to add new functionality and intends to have social media recording and analysis on the platform shortly.

Revenues have traditionally been from customised projects and artec can deliver both onsite and hosted (cloud) solutions. The company delivers its hosted cloud solutions from a large co-located datacentre in Germany. Revenues are split roughly by half direct sales and half indirect through partners including WTG Westfälische Telefon-Gesellschaft. Historically, video surveillance was the predominant target market, although the focus has been shifting to media analysis systems. This is due to the Chinese domination of video surveillance with commoditised products (although artec has found a new niche in public sector security after recent terror attacks), along with artec's recent successes in the media analysis systems end market.

Competitors in media analysis include industry giant IBM Watson, Palantir, a private US company co-founded by billionaire Peter Thiel and Veritone (Nasdaq: VERI), a small Nasdaq company that is probably artec's closest quoted peer. We note that European regulation, including the EU's General Data Protection Regulation (GDPR), makes it increasingly difficult for foreign peers to compete. Additionally, within the public security segment, European authorities strongly prefer to deal with European suppliers.

FY18 annual results

artec recorded a strong 2018, with revenues doubling to €2.9m and the group returning to a small operating profit (EBIT) of €33k from a €776k loss in FY17. Management says that excluding one-off costs relating to the capital increase and legal fees, the EBIT margin was c 10%. The medium-term goal is the lift the EBIT margin to c 15%. An estimated 10% of revenues, or c €300k, are recurring, representing a combination of cloud revenues and support contracts and there remains a clear focus on boosting scalable cloud revenues. Although management has not offered any guidance for FY19, it is clearly buoyant on the outlook for the business.

Significantly, artec received a number of important reference orders during the year, which boosts the potential for the future growth. In addition, a major US competitor, VDMS (a unit of the US telecom giant, Verizon) unexpectedly declared end-of-sale and end-of-life for the Volicon Observer product line. This provides additional possibilities for artec if Volicon's European customers look to the market for an alternative solution. Volicon Observer is a broadcast monitoring and compliance product in the media space and is transitioning its customers to a competing solution called SnapStream. artec's management is deciding its plans to target the Volicon's customer base in Europe, which would likely involve a fresh round of investment including expansion of headcount. We note that artec is not interested in targeting the US market.

In February 2018, artec undertook a 10% capital increase, raising c €0.9m to provide working capital to deliver on major contract wins. The financing slightly outweighed the modest operating cash outflow along with investing activities and the group ended the year with a small cash position of €46k, up from zero a year earlier. artec has no financial liabilities and its equity ratio increased over the period from 86% to a very strong 93%.

In early FY18, artec announced three major contracts, including XENTAURIX contracts with a major German publishing house and a German state media office and a combined MULTIEYE/ XENTAURIX contract win with the German ministry of the interior. Other FY18 customer wins included a Luxembourg security agency that has ordered an in-house cloud solution for active video management and a local authority in Germany that ordered artec face recognition (MULTIEYE face) for use as an offline face-recognition system to analyse video archives at speeds of up to 12 times during searches. New business momentum continues, with the group having attained five of the 14 German state media offices as customers. It has acquired an ex-Volicon customer in France and expanded its offering with a customer in Qatar.

Exhibit 1: Financial summary

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18
Year ended 30 September	HGB	HGB	HGB	HGB	HGB	HGB	HGB	HGB
Income statement (€000's)								
Revenue	1,750	2,220	1,832	2,436	3,469	2,475	1,462	2,936
Operating profit (loss)	(203)	175	(424)	108	637	(415)	(776)	33
Operating margin	(11.6%)	7.9%	(23.1%)	4.4%	18.4%	(16.8%)	(53.1%)	1.1%
Pre-tax profit (loss)	(169)	205	(410)	108	636	(414)	(782)	28
EPS	0.08	0.05	(0.11)	0.24	0.22	(0.13)	(0.33)	0.01
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Balance Sheet (€000's)								
Total non-current assets	1,206	1,610	1,537	1,797	1,461	1,959	2,196	2,433
Total current assets	918	729	1,159	566	1,827	1,905	1,312	1,713
Total assets	2,125	2,338	2,696	2,363	3,288	3,864	3,508	4,146
Total non-current liabilities	0	0	0	0	(57)	(71)	(83)	(93)
Total current liabilities	(104)	(149)	(408)	(276)	(202)	(90)	(523)	(174)
Total liabilities	(104)	(149)	(408)	(276)	(259)	(161)	(606)	(267)
Net Assets	2,021	2,190	2,288	2,087	3,029	3,703	2,902	3,879
Cash flow								
Net cash from operating activities	270	(116)	271	227	963	(290)	208	(136)
Net cash from investing activities	(345)	(156)	(328)	(331)	(506)	(706)	(595)	(617)
Net Cash from financing activities	1	64	51	104	(218)	989	154	798
Net Cash Flow	(74)	(208)	(6)	(1)	239	(7)	(233)	45
Cash & cash equivalent end of year	215	8	2	1	240	233	0	46

Source: Company accounts

Evolving business model

artec is targeting two primary markets – security and media and broadcast – using its complementary software platforms. artec's USP is that it can offer similar technologies, such as face recognition, to these two sectors and it does not see competitors offering in both sectors. artec is targeting state agencies and public authorities in the DACH countries with a law enforcement video surveillance management system and video intelligence applications. It is also offering scalable cloud/SaaS offerings to the media and broadcast sector. The cloud solution is the preference over project-based solutions, which require additional headcount.

Customers will typically sign long-term (three- to four-year) contracts when the software is installed on-premise. artec now also offers a pay as you go (PAYG) model and it is evolving a hybrid approach. Under the PAYG model, customers upload videos to the cloud-based platform for analysis. artec anticipates monthly revenues in the range of €1k to €25k per customer. The PAYG solution involves minimal investment from the customer while in-house solutions typically require a tender. Consequently, management is confident it can grow the cloud revenue to €1.2m in the near future. artec can also deliver on larger contracts, as exemplified by its customer in Qatar, which has

increased the number of channels it takes from 400 to 520; artec can deliver on substantially more channels.

With regard to technology, artec offers a buy, build, partner approach – as well as developing some of its own IP, it will partner other software vendors to take advantage of established solutions that can be bolted on to its MULTIEYE and XENTAURIX platforms and will consider acquiring small vendors with innovative solutions.

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