

TXT e-solutions

H114 results

Growing international presence

TXT saw 4.7% revenue growth in H114, with international revenues growing to 58% of the total from 54% in 2013. TXT Perform felt the impact of a slowdown in the luxury and fashion market in Q2. We have revised our forecasts to reflect lower licence revenues in FY14; this drives EPS cuts of 13.0% in FY14 and 4.8% in FY15. The company continues to invest in product development and recent initiatives in North America should support further growth in international revenues.

Year end	Revenue (€m)	PBT* (€m)	FD EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/12	46.5	4.2	0.37	0.20	20.6	2.6
12/13	52.6	4.8	0.45	0.25	16.9	3.3
12/14e	54.9	4.8	0.37	0.26	20.6	3.4
12/15e	60.3	6.8	0.50	0.27	15.2	3.5

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

H114 results reflect Q2 slowdown

H114 revenue growth of 4.7% y-o-y was made up of growth in TXT Perform of 8.1% and a 0.1% decline in TXT Next. The higher proportion of service revenues in H114 resulted in a lower gross margin of 51.0% versus 52.8% in H113. In Q2, margins were also affected by non-recurring costs relating to two Perform projects. Higher operating costs (+€0.8m y-o-y) reflected increased sales and marketing activity, resulting in EBITDA of €2.5m versus €3.1m in H113. In addition, TXT benefited from non-recurring income of €1.5m, retention of part of the Maple Lake purchase price as two of the original sellers left before the agreed lock-in period.

Changes to estimates

TXT Perform saw longer sales cycles in Q214, resulting in weaker licence sales than in Q114. We have reduced our FY14e revenues to reflect this weakness, but assume that licencing picks up from Q3, as pipeline deals start to convert. Reflecting a higher proportion of services revenues, gross margins are forecast to be lower in FY14/15. We have reduced our operating expense assumptions for H214 reflecting lower marketing spend (as TXT's conferences tend to be in H1) and the quieter holiday period in Europe in Q3. We reduce our normalised EPS by 13.0% in FY14e (this excludes the €1.5m non-recurring income) and 4.8% in FY15. Our net cash forecast increases after incorporating the €1.5m retention.

Valuation: Supported by strong cash position

The stock trades on a P/E of 20.6x FY14e and 15.2x FY15e normalised EPS. This is at a discount to global supply chain software vendors and at a premium to European IT services companies. The company has a strong cash position and we forecast a dividend yield of at least 3% for FY14 and FY15. To see upside from this point, we would need to see that recent investment in North America is driving new business, demand from the European retail market is recovering, operating profitability is improving or TXT Next is returning to growth.

Software & comp services

11 August 2014
Price €7.64

Market cap €80m

Net cash (€m) at end H114	6.6
Shares in issue	10.4m
Free float	64%
Code	TXT
Primary exchange	Borsa Italiana (STAR)
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(5.4)	(19.2)	43.1
Rel (local)	2.4	(8.2)	27.0
52-week high/low		€11.9	€5.1

Business description

TXT e-solutions has two divisions: TXT Perform provides software solutions for supply chain management in the international retail and consumer-driven industrial sectors; and TXT Next provides IT, consulting and R&D services to Italian aerospace, high-tech manufacturing, banking and finance customers.

Next event

Q3 results	5 November 2014
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Investment summary

Company description: Specialist software solutions

TXT e-solutions is an Italian-headquartered software and services company. TXT operates through two divisions, TXT Perform (60% of FY13 revenues) and TXT Next (40% of FY13 revenues). TXT Perform develops, supplies and installs supply chain management software, specialising in fashion, luxury and retail. TXT Next is a software solutions and services business, focused on the aerospace and defence, high-tech manufacturing and banking and finance segments, primarily in Italy. The group plans to drive growth through greater internationalisation (currently more than 50% of revenues are generated outside Italy), cross-selling and product development, and may make bolt-on acquisitions in both divisions.

Financials: Earnings revised to reflect weaker Q2

We have reduced our FY14 revenue forecast to reflect licensing weakness in Q2, but assume that licensing picks up from Q3, as pipeline deals start to convert. Reflecting a higher proportion of services revenues, gross margins are lower in FY14e/15e. We have reduced our operating expense assumptions for H214e reflecting lower marketing spend (as TXT's conferences tend to be in H1) and the quieter holiday period in Europe in Q3. After incorporating the €1.5m retention, our net cash forecast increases to €10.8m by the end of FY14.

Exhibit 1: Changes to forecasts

	EPS (€)			PBT (€m)			EBITDA (€m)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2014e	0.43	0.37	(13.0)	5.5	4.8	(12.7)	6.6	6.0	(8.9)
2015e	0.53	0.50	(4.8)	7.2	6.8	(5.6)	8.0	7.7	(4.0)

Source: Edison Investment Research

Valuation: Supported by strong cash position

On our revised earnings forecasts, TXT trades at a premium to European IT services companies, but at a discount to specialist SCP software suppliers. Based on the growth and profitability profiles of both groups, we would expect TXT to trade somewhere in the middle of the two groups. The mix of revenues is shifting in favour of the higher margin TXT Perform business, which should drive up multiples over time. We note a forecast dividend yield of at least 3%, supported by TXT's strong cash position. Triggers for share price appreciation include large licence wins in TXT Perform, evidence of growing North American market share, resumption of growth in TXT Next and evidence that operating profitability is improving.

Sensitivities: Demand, competition, currency

- **General economic activity:** Sales in both divisions will be influenced by the health of the economy. The TXT Next business has more exposure to the Italian economy, although the international customer base of many of its customers reduces this exposure.
- **Competition:** TXT Perform competes against larger software companies with greater resources for R&D and sales. There is also the risk that TXT Perform could lose business to ERP vendors that include SCP software in their solutions, although the specialist nature of TXT's solutions should reduce this risk.
- **Acquisition risk:** TXT plans to make further acquisitions, adding potential integration risk.
- **Currency:** The majority of TXT's revenues and costs are incurred in euros. There is some exposure to sterling, and US dollar exposure will increase with the acquisition of Maple Lake. In both cases, the impact will be mitigated by the costs of staffing local offices in the same currency as revenues.

Company description: Specialist software solutions

Company background

TXT e-solutions was formed in 1989 as a software and solutions vendor and listed on the STAR segment of the Borsa Italiana in 2000. The company operates through two divisions, TXT Perform (60% of FY13 revenues) and TXT Next (40% of FY13 revenues). TXT Perform develops, supplies and installs supply chain management software, specialising in fashion, luxury and retail. The business has grown organically and via acquisitions in Germany (2004), the UK (2008) and North America (Maple Lake acquisition in 2012). TXT Next is a software solutions and services business, focused on the aerospace and defence, high-tech manufacturing, and banking and finance segments, primarily in Italy. This business has grown organically.

Group strategy

Group strategy is to continue to drive revenue growth in the two businesses via greater internationalisation (in H114 58% of revenues were generated outside Italy), cross-selling and product development. The company continues to consider acquisitions, particularly in the TXT Perform business. We discuss the individual divisional strategies in more depth later in the report.

Management

TXT is run by a long-established team: the chairman is the original founder of the company and the CEO joined TXT in 1994. Divisional heads have many years' experience with the company. TXT Perform is headed by Andrea Cencini, who joined TXT in 1989 and has performed various roles in the business. TXT Next is headed by Paolo Colombo, who has been with TXT since it was founded and has built the division into its current structure.

TXT Perform: Supply chain solutions for retail

TXT Perform develops, sells and installs supply chain planning software. The division has more than 200 consultants operating out of 15 sales and delivery offices across Europe (France, Germany, Italy, Spain and the UK), Canada, the US and Australia.

Product offering

TXT's software solutions are based on its TXTPERFORM platform, developed to work with Microsoft SQL, Excel and Sharepoint. TXT Perform offers a suite of products across three main functional areas:

- Integrated retail planning solutions (c 75% of divisional revenues).
- Product Lifecycle Management (PLM) for retail (c 15% of divisional revenues)
- Sales and operations planning (c 10% of divisional revenues).

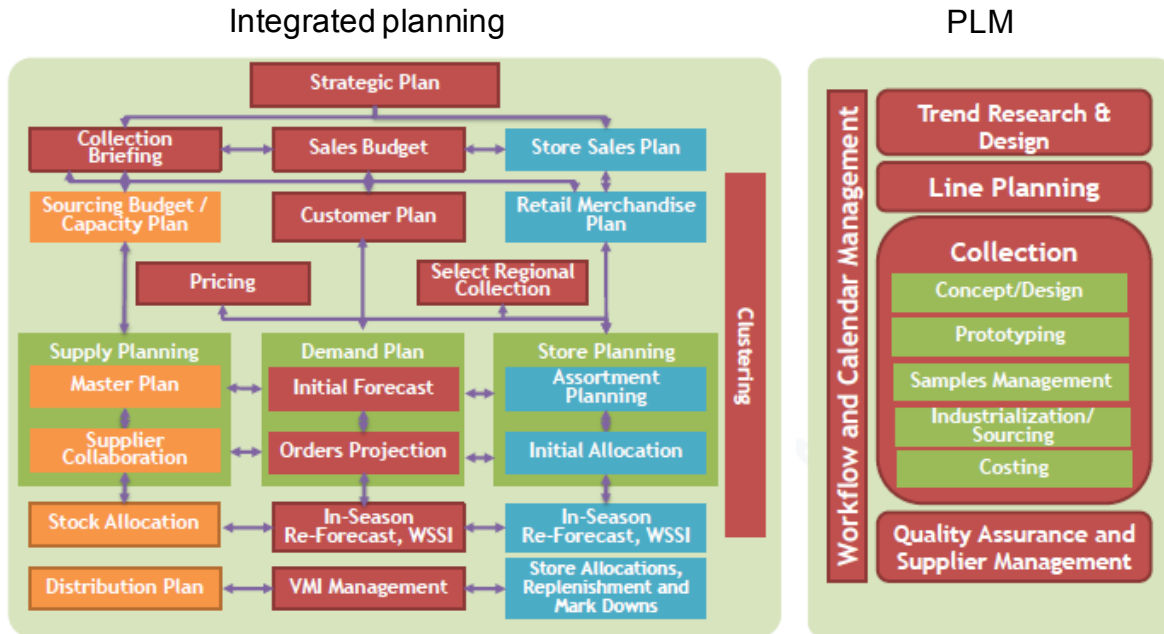
Integrated retail planning

TXT Perform's roots are in the retail sector, giving it many years' experience in this area and a product range that has been tailored to the industry's specific needs. Exhibit 2 shows TXT's comprehensive solution, although customers can choose to buy modules within it, such as Sales Planning or Merchandise & Assortment Planning. The software is designed to enable users to see the implications of each decision they make on both operational and financial KPIs, with 'what-if' analyses possible for a variety of factors such as channel, product, geography and brand.

Product lifecycle management

In the retail sector, PLM software is used to bring order to the collection-development process. The software is designed to align all stakeholders, eg merchandisers, designers, buyers, suppliers, product managers and developers, to reduce the time and cost involved in developing a new collection. TXT's solution (see Exhibit 2) operates in a single web environment, and is Sharepoint-based, enabling all stakeholders to participate in and/or review the process wherever they are. The software is integrated with TXT's integrated retail planning solution.

Exhibit 2: Integrated planning and PLM software solutions



Source: TXT e-solutions

Sales and operations planning

TXT's market focus is CPG and consumer-facing industrials such as Kraft, Eckes Granini and elica (cooker hoods). Exhibit 3 shows the functionality of TXT's sales and operations planning solution.

Exhibit 3: Sales and operations planning functionality



Source: TXT e-solutions

Blue chip customer base

Exhibit 4 demonstrates the strength of TXT's customer base in its chosen markets. TXT Perform has more than 350 customers. The company targets Tier 1 customers, ie those with annual revenues of more than €250m, with the sweet spot being those over €500m. Overall, roughly two-thirds of annual revenues come from existing customers (one-third of licence sales and two-thirds of services revenues), highlighting the company's ability to cross- and up-sell. The division won 15 new customers in 2013 and customers won year to date include Otto (Germany), La Halle (France), The White Company (UK), Pandora (Denmark) and Krones (Germany). The company has also won licence extensions this year with existing customers including Cotton On, Damartex, Dior, Greencore, Lindex and Starboard Cruise Services.

Exhibit 4: Selected customers

Luxury		Global Brands		Fast Fashion		Mixed Goods	
Burberry	Gucci	adidas	Ecco	Aéropostale	Kenneth Cole	Apollo Optik	Monoprix
Céline	Loewe	Bata	Lacoste	Asos	Lindex	Auchan	Pandora
Dior	LVMH	Camper	Levi's	Cotton On	Steve Madden	Damart	Redcats
Donna Karan	Marc Jacobs	Desigual	North Face	Fat Face	Tom Tailor	Game	Safilo
Dunhill	Prada	Diesel	Tod's	Hobbs	Topshop	Manor	The White Company

Source: TXT e-solutions

Supply chain management software market

The supply chain management software market was worth \$8.9bn in 2013 (source: Gartner) and grew 7.3% y-o-y. Gartner expects the market (ex-procurement software) to continue to grow at a CAGR of 9.9% from 2013 to 2018. The top five vendors (SAP, Oracle, RedPrairie [incorporating JDA Software], Manhattan Associates and Epicor) made up close to 50% of the market. The remainder was made up of a large number of small and medium-sized vendors, including TXT. The market splits into two broad areas: supply chain planning and supply chain execution software. TXT specialises in supply chain planning (SCP) software. Gartner estimates that the SCP software market was worth \$3.4bn in 2013 (+10% y-o-y).

SAP and Oracle dominate this market and the other major player is JDA Software, acquired by RedPrairie at the end of 2012. TXT is focused on specific areas of the SCP market: fashion, luxury and retail integrated planning solutions, and sales and operations planning (S&OP) software for the CPG and industrial sectors. Based on the countries and niche segments in which TXT operates, the company estimates that it has an addressable software licence market of c €300m and therefore a market share of c 5%.

The retail market has a number of characteristics that drive the need for specialised SCP solutions:

- In fashion, the speed at which new collections are required is increasing. Customers of high-fashion stores expect multiple collections each year, with new lines expected on an ongoing basis.
- Outsourced manufacturing of apparel and footwear, particularly to China and Vietnam, makes it harder to have visibility and control over suppliers.
- The market is highly price competitive, so any advantage that can be gained at the cost-of-goods level is crucial.
- Retailers want to provide high levels of customer service and to do so need to be able to have the right product in the right place at the right price.
- The ability to sell products through different channels (multi-channel) is becoming a necessity.

Competitors include companies that develop standalone supply chain software that can be integrated with a customer's existing ERP software, or companies that develop supply chain modules as part of their ERP offering. TXT software is designed to integrate with the main ERP vendors' software, including SAP and Microsoft. For markets such as retail, often the supply chain

functionality within an ERP system is not sufficiently deep to maximise the benefits of the software. For all products, TXT also competes with inertia, ie the customer continues to use their own spreadsheets and other manual processes.

In recent Gartner Magic Quadrant reports, TXT has achieved challenger status for supply chain planning (high ability to execute) and visionary status for retail assortment management applications (high level of innovation). For S&OP, Gartner has given TXT a 'positive' rating, alongside Oracle, JDA Software and a small specialist provider, Steelwedge Software.

Growth strategy

The division is seeking to grow through several routes:

- Internationalisation: Business is generated across the main geographies in which TXT Perform is based, with Italy making up only 15% of FY13 revenues (UK & Nordics 21%, France 19%, Germany 15%, North America 15%, Spain 4% and other countries 11%). The division is keen to increase market share in North America (in the short to medium term) and expand into Asia in the longer term. TXT Perform currently does some business in Asia-Pacific for its European and North American customers but would ultimately like to target Asia-headquartered retailers.
- Expansion into other retail segments and by targeting smaller retailers.
- Cross-selling/up-selling: TXT Perform seeks to sell PLM to its retail customers – around 30% of customers buying integrated planning software for fashion also buy the PLM solution. TXT Perform will also require licence extensions when the customer increases the number of users, processes, product categories or geographies. The products can be used for one or more channels (retail, wholesale, online) and increasingly customers are using across all channels.
- Extend product features and functionality: In 2013, TXT launched TXT On-Cloud, TXT Mobile and four new mobile PLM and planning modules. The company is developing in-memory processing capability and social media-related solutions. TXT recently introduced its AgileFit methodology, which provides standardised implementation models for selected verticals. This should accelerate the implementation process and potentially enhance margins.

Progress in North America

In 2012, TXT acquired Maple Lake, a retail-focused SCP software provider headquartered in Canada with significant business across the US, as well as Canada, Europe and Australia. At the date of acquisition, the business had nearly 50 customers, many of them top-tier retailers such as adidas, Arcadia Group, Barneys New York, and Levi Strauss & Co. TXT will continue to support existing Maple Lake software for five years. The acquisition gives TXT local presence in North America, and from a product perspective, strengthens the TXT Perform platform. To accelerate North American sales, TXT has hired several new sales and marketing employees; this includes the January hiring of Peter Charness as senior vice president of North America who will also take on the role of chief marketing officer. In Q114, TXT established a US subsidiary, additional to the subsidiary in Toronto (ex-Maple Lake) and in Q314 appointed Jean-Philippe Vorsanger as COO of North American operations (based in Toronto).

TXT Next: Systems engineering specialist

TXT Next is the engineering division of TXT, which provides specialised software solutions and services to four end markets: aerospace & defence, automotive, high tech and banking & finance. The first three sectors are served through the Aerospace & High Tech Manufacturing (A&HT) division (66% of TXT Next H114 revenues), and the Banking & Finance (B&F) division generated 28% of TXT Next H114 revenues. Exhibit 5 shows the key areas supported in each end market.

Exhibit 5: TXT Next business activities

	Aerospace & defence	Automotive	High tech	Banking & finance
Mission-critical systems software development	x	x	x	
Simulation and modelling	x			
Complex manufacturing	x	x		
Business intelligence & business process management	x	x	x	x
Independent verification & validation (IV&V)	x	x	x	x
IT governance and quality	x	x	x	x
Enterprise applications				x

Source: TXT e-solutions

The division has a customer base of more than 30 companies. Although most of the work is project based and therefore not recurring in nature, TXT has a very loyal customer base that provides repeat work.

The A&HT division's revenues are generated from simulation and training (c 40%), embedded software (c 40%) and digital manufacturing (c 20%). The B&F division generates c 50% of revenue from IT governance (testing and software quality), c 30% from analysis and design (intranet and software innovation) and c 20% from application maintenance. B&F's target market is the Italian banking market, which is made up of c 45 medium-sized to large banks, of which five to six are top tier. Exhibit 6 gives examples of the type of work undertaken by both divisions.

Exhibit 6: Examples of work undertaken

A&HT division		B&F division	
Client	Project	Client	Project
Agusta Westland	Bespoke on-board software for EH101 helicopter	ING Direct	Software testing
	Software for helicopter flight simulator	Banco Popolare	Intranet development & application maintenance
Aircraft manufacturers	Digital manufacturing	Credito Valtellinese	Intranet development & application maintenance
Magneti Marelli	In-car multi-media devices	Banca Mediolanum	Software IV&V
bticino	IT governance for door-entry systems	Webank.it	Analysis and design of front-end applications
Siemens	Customised automation software	Banca Popolare di Milano	Analysis and design for systems compliance

Source: TXT e-solutions

Competitive environment

The division's competition is from customers' in-house R&D and IT departments, as well as from other local system integrators. The company estimates it has a 5-7% market share in system engineering in Italy. TXT Next has been a beneficiary of the trend to outsource, which gives the customer greater flexibility on cost and better access to specialist skills. Once a customer has outsourced a specialist area of R&D or IT, it is usually very difficult to bring it back in house, as the in-house knowledge and expertise will have diminished. TXT Next has worked closely with the majority of its customer base for many years, creating a strong partnership and demonstrating its specialist expertise.

Growth strategy

TXT Next is based in Italy and less than 10% of FY13 revenues were generated outside Italy, generally arising from a 'follow-my-customer' strategy. The main focus is on developing new solutions and expertise and improving the profitability of the business. The division is looking to expand the aeronautics business internationally (with the focus on embedded electronics, simulation and training and digital manufacturing), to grow the automotive and rail businesses, (initially in Italy) and to grow the software testing business in the Italian banking sector. The division will expand internationally where customers demand it, and is considering acquisitions within Europe to diversify the customer base and add local presence.

Sensitivities

Our forecasts and TXT's share price will be sensitive to the following factors:

- **General economic activity:** Sales in both divisions will be influenced by the health of the economy. The TXT Next business has more exposure to the Italian economy, although the international customer base of many of its customers reduces this exposure.
- **Competition:** TXT Perform competes against larger software companies with greater resources for R&D and sales. There is also the risk that TXT Perform could lose business to ERP vendors that include SCP software in their solutions, although the specialist nature of TXT's solutions should reduce this risk.
- **Acquisition risk:** TXT plans to make further acquisitions, adding potential integration risk.
- **Currency:** The majority of TXT's revenues and costs are incurred in euros. There is some exposure to sterling and the acquisition of Maple Lake has increased US and Canadian dollar exposure. The impact is mitigated by the costs of staffing local offices in the same currency as revenues.

Financials

Review of H114 results

Exhibit 7: Half-yearly results highlights			
	H113	H114	Change (%)
Revenues*	26.3	27.5	4.7
TXT Perform	15.4	16.6	8.1
TXT Next	10.9	10.9	(0.1)
Gross margin*	52.8%	51.0%	(1.8)
EBITDA*	3.1	2.5	(19.6)
EBITDA margin*	12.0%	9.2%	(2.8)
Normalised EBIT*	2.7	2.0	(23.7)
Normalised EBIT margin*	10.1%	7.4%	2.8
Reported EBIT	2.5	3.4	34.4
Reported EBIT margin	9.6%	12.3%	2.7
Net cash	6.8	6.6	(2.2)

Source: TXT e-solutions. Note: *Excludes €1.5m non-recurring income received in Q214.

TXT grew H114 revenues 4.7% y-o-y. TXT Perform revenues grew by 8.1% whereas TXT Next saw a small 0.1% decline. The higher proportion of service revenues in H114 compared to H113 resulted in a lower gross margin. In Q2, margins were also affected by non-recurring costs of €0.4m relating to two Perform projects. Operating costs (excluding depreciation and amortisation) increased €0.8m y-o-y, reflecting increased sales and marketing activity. Two of the original Maple Lake founders/sellers left in Q214, before the end of the three-year lock-in period agreed at the time of the deal. This resulted in TXT receiving a one-off payment of €1.5m which was an agreed retention from the purchase price. We have treated this as an exceptional item.

TXT Perform

FY13 revenues were generated from licences (18%), maintenance and support (22%) and services (60%). Maintenance has a high retention rate of c 98%. Software is proprietary, so licence revenues generate GMs close to 100%. Taking into account maintenance and support revenues and services revenues, the division typically generates an overall GM of 60-65%. H114 revenues grew 8.1% y-o-y. Perform's H114 service revenues grew 12% y-o-y whereas licence revenues were only 2% higher. Perform had a strong licensing quarter in Q114 (+8% y-o-y) but longer sales cycles resulted in lower licence sales in Q2 (-4% y-o-y). We reduce TXT Perform revenues by 4.1% for FY14

(reflecting the weak licence revenues in Q2); FY15 is substantially unchanged. GMs reflect the higher proportion of service revenues (FY14e from 62.2% to 60.2%, FY15e from 61.9% to 60.5%).

Exhibit 8: TXT Perform forecasts

€m	FY09	FY10	FY11	FY12	FY13	FY14e	FY15e
Licences & maintenance	6.5	8.6	8.8	10.2	12.8	13.2	14.6
Projects & other income	11.1	12.5	13.3	16.2	18.9	20.6	23.0
Total revenue	17.5	21.1	22.1	26.4	31.7	33.8	37.6
Growth		20.6%	4.4%	19.4%	20.1%	6.8%	11.2%
Gross margin	51.9%	58.0%	60.9%	62.5%	62.6%	60.2%	60.5%

Source: TXT e-solutions, Edison Investment Research

TXT Next

TXT Next revenues fell 0.1% y-o-y in H114, with revenues down 1.3% y-o-y in Q1 and up 1.2% in Q2. As flagged after Q114 results, TXT Next revenues were affected by the delay in the start-up of new projects at one customer, which should be recovered in Q3 and Q4. We have reduced our FY14 revenue forecast by 0.5%, which implies H214 revenues grow 1.8% y-o-y/-6.1% h-o-h, to achieve FY14 revenue growth of 0.8% (we note that the business tends to show seasonal weakness in Q3 due to the holiday period in Europe). We forecast 7.9% revenue growth for FY15 (0.3% reduction in previous revenue forecast). As a predominantly service-based business, TXT Next generates gross margins in the range 35-40%.

Exhibit 9: TXT Next forecasts

€m	FY09	FY10	FY11	FY12	FY13	FY14e	FY15e
Licences & maintenance	0.2	0.2	0.2	0.1	0.1	0.1	0.1
Projects & other income	13.4	16.1	17.9	20.0	20.8	21.0	22.7
Total revenue	13.6	16.3	18.1	20.1	20.9	21.1	22.7
Growth		20.2%	10.7%	11.5%	3.8%	0.8%	7.9%
Gross margin	37.3%	39.4%	39.7%	38.1%	37.6%	38.9%	37.1%

Source: TXT e-solutions, Edison Investment Research

Changes to forecasts

Our revised forecasts reflect weaker licence sales in TXT Perform and lower operating expenses.

Exhibit 10: Changes to forecasts

	FY14 old	FY14 new	Change (%)	FY15e old	FY15e new	Change (%)
Revenues* (€m)	56.4	54.9	(2.7)	60.4	60.3	(0.1)
TXT Perform	35.3	33.8	(4.1)	37.6	37.6	0.1
TXT Next	21.2	21.1	(0.5)	22.8	22.7	(0.3)
Gross margin*	53.4%	52.0%		52.2%	51.7%	
Gross profit*	30.2	28.6	(5.3)	31.5	31.2	(1.0)
EBITDA* (€m)	6.6	6.0	(8.9)	8.0	7.7	(4.0)
EBITDA margin*	11.6%	10.9%		13.3%	12.8%	
Normalised EBIT* (€m)	5.6	5.0	(11.1)	7.3	6.9	(4.9)
Normalised EBIT margin*	9.9%	9.0%		12.1%	11.5%	
Normalised net income* (€m)	4.7	4.0	(13.1)	5.7	5.5	(5.0)
Normalised EPS* (€)	0.43	0.37	(13.0)	0.53	0.50	(4.8)
Net cash (€m)	10.3	10.8	5.2	13.2	13.3	0.9
Dividend (€)	0.26	0.26	0.0	0.27	0.27	0.0

Source: Edison Investment Research. Note: *Excludes €1.5m non-recurring income in Q214.

Valuation

On our revised earnings forecasts, TXT trades at an EV/Sales and P/E premium to European IT services companies, but at a discount to specialist SCP software suppliers. Based on the growth and profitability profiles of both groups, we would expect TXT to trade somewhere in the middle of the two groups. The mix of revenues is shifting in favour of the higher margin TXT Perform, which

should drive up multiples over time. We note a forecast dividend yield of at least 3%, supported by TXT's strong cash position. Triggers for share price appreciation include large licence wins in TXT Perform, evidence of growing North American market share, resumption of growth in TXT Next and evidence that operating profitability is improving.

Multiples-based valuation

As the business is a combination of software and IT services, we include the valuation multiples for international SCP software companies, as well as European IT services providers.

Exhibit 11: Peer group valuation												
Company	Share price	Market cap (m)	Rev growth		EBIT margin		EBITDA margin		EV/Sales (x)		P/E (x)	
			CY	NY	CY	NY	CY	NY	CY	NY	CY	NY
TXT	€7.64	€80	4.4%	9.9%	9.0%	11.5%	10.9%	12.8%	1.4	1.3	20.6	15.2
Software companies with SCM software offerings												
American Software	\$9.18	\$259	9.8%		15.5%		21.2%		1.6		21.9	
Descartes	\$13.37	\$1,004	14.7%	12.4%	15.7%	18.7%	29.9%	30.8%	5.5	4.7	53.5	40.5
Kinaxis	C\$15.09	C\$356	23.4%	22.6%	16.3%	16.6%	19.9%	21.8%	4.9	4.0	39.7	34.3
Manhattan Associates	\$30.67	\$2,303	14.7%	8.3%	28.3%	28.9%	29.6%	30.3%	4.5	4.0	27.4	24.7
MICROS Systems	\$67.82	\$5,074	6.4%	2.4%	21.3%	22.4%	22.1%	24.1%	3.0	3.0	24.3	24.3
Oracle	\$40.21	\$179,109	4.8%	4.6%	48.2%	48.6%	51.4%	51.4%	4.3	4.0	12.7	11.7
SAP	€57.67	€68,829	3.2%	6.7%	31.1%	32.3%	34.3%	35.5%	3.9	3.6	17.0	15.5
Totvs	R39.78	R6,485	10.4%	10.3%	23.2%	24.3%	25.8%	26.6%	3.6	3.2	22.2	18.7
Average			10.9%	9.6%	24.9%	27.4%	29.3%	31.5%	3.9	3.8	27.3	24.2
European IT services companies												
AtoS	€55.71	€5,467	0.5%	3.4%	6.7%	7.4%	11.1%	11.8%	0.6	0.6	13.0	11.8
Cap Gemini	€52.21	€8,317	3.2%	3.8%	8.5%	9.0%	10.7%	11.3%	0.8	0.7	15.0	13.4
Computacenter	£6.01	£836	2.1%	2.7%	2.7%	2.8%	3.7%	3.8%	0.3	0.3	12.7	12.0
Devoteam	€17.78	€159	-12.0%	-1.2%	4.5%	5.9%	5.5%	6.8%	0.3	0.3	19.1	13.4
Engineering II	€38.05	€464	5.1%	4.3%	9.6%	9.8%	12.4%	12.5%	0.5	0.5	10.2	9.6
Sopra Group	€79.47	€947	8.7%	4.8%	8.1%	8.7%	9.7%	10.2%	0.7	0.7	12.0	10.7
SQS	£5.47	£167	16.1%	11.3%	7.2%	7.8%	9.4%	9.8%	0.8	0.7	15.6	13.1
Average			3.4%	4.2%	6.8%	7.3%	8.9%	9.5%	0.6	0.5	14.0	12.0

Source: Thomson Reuters, Edison Investment Research. Note: Priced as at 6 August.

Recent M&A

M&A within the retail and planning software market continues to be active. Dassault Systèmes announced in July that it plans to buy Quintiq for €250m; Quintiq is a Dutch privately-owned provider of S&OP software. This values the business at c 3.4x CY13 revenues (CY13 revenues grew 26%; profitability has not been disclosed). In June, Oracle announced that it was buying MICROS, the Nasdaq-listed provider of retail and hospitality point of sales software and hardware. Oracle is paying \$68/share in cash, valuing MICROS at \$5.3bn – this equates to an EV/Sales multiple of 3.0x FY15e (y/e June 2015) and a P/E multiple of 24.4x FY15e. While this is not strictly a supply chain planning company, it highlights the attractiveness of the retail software market to large software companies. In May, Logility (owned by American Software) announced it had acquired MID Retail, a privately-owned US provider of retail allocation and merchandise planning solutions.

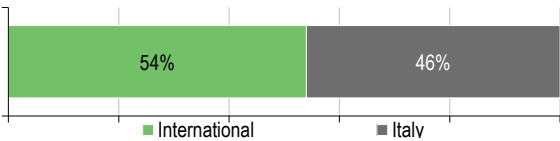
Reverse DCF

We have performed a reverse 10-year DCF to calculate what we believe the market is factoring into the current share price. Using a WACC of 10%, long-term growth of 2%, working capital/sales of 1.0% and capex/sales of 1%, a revenue CAGR of 4.4% for 2016-23 and average EBITDA margins of 12.9% from FY16-23 are required to reach the current share price. Based on forecast market growth for SCP software and IT services, this appears overly harsh in terms of revenue growth and implies minimal margin expansion post-2015.

Exhibit 12: Financial summary

	€'000s	2010	2011	2012	2013	2014e	2015e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		37,458	40,138	46,499	52,560	54,899	60,332
Cost of sales		(18,757)	(19,522)	(22,351)	(24,854)	(26,340)	(29,149)
Gross profit		18,701	20,616	24,148	27,706	28,559	31,183
EBITDA		2,769	4,397	5,322	6,263	5,982	7,703
Operating Profit (before amort and except)		(776)	843	4,283	5,256	4,960	6,931
Amortisation of acquired intangibles		0	0	0	(300)	(285)	(285)
Exceptionals and other income		13	(4,581)	939	0	1,500	0
Other income		0	0	0	0	0	0
Operating Profit		(763)	(3,738)	5,222	4,956	6,175	6,646
Net Interest		(198)	72	(37)	(435)	(200)	(100)
Profit Before Tax (norm)		(974)	915	4,246	4,821	4,760	6,831
Profit Before Tax (FRS 3)		(961)	(3,666)	5,185	4,521	5,975	6,546
Tax		255	(591)	(188)	121	(896)	(1,309)
Profit After Tax (norm)		(719)	324	4,092	4,942	4,046	5,465
Profit After Tax (FRS 3)		(706)	(4,257)	4,997	4,642	5,079	5,237
Average Number of Shares Outstanding (m)		10.3	10.1	10.0	10.5	10.4	10.4
EPS - normalised (c)		(7)	3	41	47	39	52
EPS - normalised fully diluted (c)		(6)	3	37	45	37	50
EPS - (IFRS) (c)		2	140	50	44	49	50
Dividend per share (c)		0.0	100.0	20.0	25.0	26.0	27.0
Gross margin (%)		49.9%	51.4%	51.9%	52.7%	52.0%	51.7%
EBITDA Margin (%)		7.4	11.0	11.4	11.9	10.9	12.8
Operating Margin (before GW and except) (%)		-2.1	2.1	9.2	10.0	9.0	11.5
BALANCE SHEET							
Fixed Assets		14,328	7,735	18,570	17,850	17,063	16,526
Intangible Assets		11,526	6,561	16,621	15,370	14,570	14,020
Tangible Assets		1,528	819	1,154	1,118	1,131	1,144
Other		1,274	355	795	1,362	1,362	1,362
Current Assets		28,876	32,145	36,769	34,914	37,563	41,115
Stocks		793	661	1,388	1,451	1,200	1,200
Debtors		21,453	15,083	19,562	18,642	20,305	22,315
Cash		6,630	14,181	15,819	14,821	16,058	17,601
Other		0	2,220	0	0	0	0
Current Liabilities		(17,719)	(14,049)	(20,651)	(17,864)	(18,507)	(19,999)
Creditors		(15,615)	(12,292)	(15,155)	(14,512)	(15,155)	(16,647)
Short term borrowings		(2,104)	(1,757)	(5,496)	(3,352)	(3,352)	(3,352)
Long Term Liabilities		(8,398)	(5,567)	(8,666)	(6,965)	(5,965)	(4,965)
Long term borrowings		(3,870)	(2,155)	(4,301)	(2,896)	(1,896)	(896)
Other long term liabilities		(4,528)	(3,412)	(4,365)	(4,069)	(4,069)	(4,069)
Net Assets		17,087	20,264	26,022	27,935	30,154	32,677
CASH FLOW							
Operating Cash Flow		9,967	19,265	2,760	7,630	6,712	7,186
Net Interest		(198)	166	(37)	(435)	(200)	(100)
Tax		255	390	64	(1,615)	(896)	(1,309)
Capex		(2,340)	(2,159)	(405)	(483)	(520)	(520)
Acquisitions/disposals		(137)	2,403	(8,450)	19	0	0
Financing		324	(106)	1,690	(755)	(269)	0
Dividends		0	(10,292)	0	(2,107)	(2,615)	(2,714)
Net Cash Flow		7,871	9,667	(4,378)	2,254	2,212	2,543
Opening net debt/(cash)		7,248	(723)	(10,266)	(6,023)	(8,575)	(10,787)
HP finance leases initiated		0	0	0	0	0	0
Other		100	(124)	135	298	0	(0)
Closing net debt/(cash)		(723)	(10,266)	(6,023)	(8,575)	(10,787)	(13,330)

Source: TXT e-solutions and Edison Investment Research

Contact details	Revenue by geography
Via Frigia, 27 20126 Milano Italy +39 02 257711 www.txtgroup.com	

CAGR metrics	Profitability metrics	Balance sheet metrics	Sensitivities evaluation				
EPS 11-15e	101.3%	ROCE 14e	12.6%	Gearing 14e	N/A	Litigation/regulatory	○
EPS 13-15e	5.3%	Avg ROCE 11-15e	13.1%	Interest cover 14e	N/A	Pensions	○
EBITDA 11-15e	15.0%	ROE 14e	13.4%	CA/CL 14e	2.1x	Currency	◐
EBITDA 13-15e	10.9%	Gross margin 14e	52.0%	Stock days 14e	8	Stock overhang	◐
Sales 11-15e	10.7%	Operating margin 14e	9.0%	Debtor days 14e	135	Interest rates	○
Sales 13-15e	7.1%	Gr mgn / Op mgn 14e	5.8x	Creditor days 14e	100	Oil/commodity prices	○

Management team	
CEO: Marco Guida Mr Guida joined TXT e-solutions from Pirelli Group in 1994. As director of international operations, he successfully led the transformation of TXT e-solutions from an Italian organisation to an international one. In 2006, he became the general manager of TXT e-solutions and was appointed CEO of TXT Group in 2009.	CFO: Paolo Matarazzo Before joining TXT in 2007, Mr Matarazzo spent seven years as head of finance, administration and control in Europe for Eurand, a company listed on NASDAQ in 2007. Before that, he worked for the Recordati Group for seven years, with responsibility for treasury management. He spent three years as an analyst in London.

Chairman: Alvisè Braga Illa
 Mr Braga Illa led the optical communications group and the network systems at the Massachusetts Institute of Technology. He directed the R&D Labs at Italtel, founded Zeltron and managed the restructuring of Ducati Energia. He founded TXT Automation Systems, sold to ABB in 1997, and TXT e-solutions in 1989.

Principal shareholders	(%)
E-business Consulting	25.1
Alvisè Braga Illa (Chairman)	13.0
Treasury shares	11.7
Marco Guida	2.1
Lazard Frères Gestions SAS	1.1
AXA Investment Managers Paris	0.8
Fideuram Investimenti SGR SpA	0.4

Companies named in this report
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