TXT e-solutions

FY16 results

Strong cash flow supports dividend boost

Software & comp services

FY16 results confirmed that the PACE acquisition has been successfully integrated and TXT Next continues to see good underlying growth. Despite weaker trading for TXT Retail in H116, TXT managed costs well to achieve profitability and cash generation ahead of our forecasts. The company continues to internationalise both businesses and we believe it could make further bolt-on acquisitions in the TXT Next business.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/15	61.5	5.7	0.40	0.25	23.2	2.7
12/16	69.2	8.1	0.55	0.30	16.9	3.2
12/17e	74.9	8.0	0.53	0.32	17.5	3.4
12/18e	77.9	8.8	0.59	0.33	15.7	3.6

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

PACE acquisition boosts FY16 performance

TXT reported revenue growth of 12.4% (1.8% organic). TXT Retail struggled with a poor trading environment in H116 and despite a pick-up in H216, saw a 1.6% revenue decline in FY16. TXT Next generated 33% growth and even without PACE, saw 6.5% organic growth. EBITDA was 3% higher than forecast and with lower than expected finance costs, the company reported normalised EPS 8.5% ahead of our forecast (+35.6% y-o-y). The company announced a dividend of €0.3 for FY16 (+20% y-o-y), ahead of our €0.26 forecast. Boosted by the PACE acquisition, international revenues grew 23% to make up 60% of FY16 revenues, up from 55% a year ago.

Minor changes to earnings forecasts

We continue to forecast revenue growth of c 8% for both divisions in FY17. Our EBITDA forecast is unchanged. Higher net interest income and lower depreciation drives an increase in our normalised EPS forecast of 7%. We introduce an FY18 forecast for 4.1% revenue growth and 10.8% EPS growth. We have increased our dividend forecast for FY17 by 18.5%. With FY16 net cash coming in €2.7m ahead of our forecast, we increase FY17 net cash by 79% to €7.2m despite the higher dividend payout.

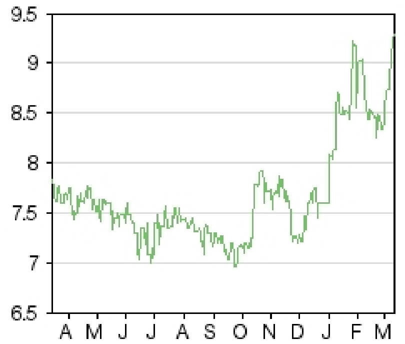
Valuation: International expansion to drive upside

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 supply chain planning (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. With the addition of PACE, the mix of revenues is shifting in favour of higher-margin licence sales, which should drive up valuation multiples over time. We also note a forecast dividend yield of more than 3%. Triggers for share price appreciation include large licence wins in TXT Retail, evidence of growing North American and Asia Pacific market share and further international wins in TXT Next. We highlight TXT's strong cash position, providing a strong position from which to undertake bolt-on acquisitions or fund internal product development.

13 March 2017

Price	**€9.29**
Market cap	**€109m**
	$1.07:€1
Net cash (€m) at 31 December 2016	5.4
Shares in issue	11.7m
Free float	45.5%
Code	TXT
Primary exchange	Borsa Italiana (STAR)
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	10.2	22.2	22.4
Rel (local)	5.5	13.0	11.9
52-week high/low		€9.3	€7.0

Business description

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

Next events

Shareholders meeting	21 April 2017

Analysts

Katherine Thompson +44 (0)20 3077 5730

Dan Ridsdale +44 (0)20 3077 5729

tech@edisongroup.com

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TXT e-solutions is a research client of Edison Investment Research Limited

Review of FY16 results

Exhibit 1: Results highlights

	FY16e	FY16	% difference	% y-o-y
Revenues (€m)	**69.3**	**69.2**	**-0.3**	**12.4**
TXT Retail	36.3	36.1	-0.7	-1.6
TXT Next	33.0	33.1	0.2	33.0
Gross margin (%)	53.3	53.7	0.4	
Gross profit	37.0	37.1	0.4	14.7
EBITDA (€m)	**8.5**	**8.7**	**3.1**	**30.9**
EBITDA margin (%)	12.2	12.6	0.4	
Normalised EBIT (€m)	**7.8**	**8.0**	**2.3**	**36.7**
Normalised EBIT margin (%)	11.2	11.5	0.3	
Normalised net income (€m)	5.9	6.4	8.5	34.8
Normalised EPS (€)	**0.50**	**0.55**	**8.5**	**35.6**
Reported basic EPS (€)	0.45	0.48	6.4	42.8
Net cash (€m)	**2.7**	**5.4**	**101.2**	**-35.0**
Dividend (€)	0.26	0.30	15.4	20.0

Source: TXT e-solutions, Edison Investment Research

TXT reported FY16 revenues in line with our forecast, showing reported growth of 12.4% and organic growth of 1.8%. Gross margins were marginally higher than forecast and operating expenses (pre-amortisation and depreciation) were slightly lower than forecast. This resulted in an EBITDA margin of 12.6%, compared to 10.8% in FY15. We have treated €0.5m in legal and M&A costs as exceptional. The company shifted to net interest income from net expense, giving a further boost at the normalised EPS level compared to our forecast. Due to good working capital management, cash flow was significantly stronger than we forecast, resulting in year-end net cash of €5.4m despite paying €5.4m for the PACE acquisition in April. The company raised its dividend 20% y-o-y to €0.30, ahead of our forecast.

Business update

TXT Retail

The division saw revenues decline 1.6% in 2016. Trading was weaker in H116 as retailers delayed investment. There was also a large licence signed in Q215 making comparisons tougher. Divisional gross margin of 63.7% was lower than the 64.2% in FY15 due to the mix of software and services.

Trading improved in the second half of the year and the company has successfully expanded its geographic reach with contracts signed in China and India. In Q416, TXT signed contracts with Not Your Daughter's Jeans – NYJD Apparel (US), Group Royer (French footwear retailer expanding in Europe, China, India and Vietnam), Charles Vögele (Swiss fashion retailer operating in Switzerland, Germany and Eastern Europe), Rusta AB (Swedish home living retailer operating in Sweden and Norway), Auchan China, Mizuno Europe (UK), Dochki Sinochki (Russian baby and child product retailer) and Stockmann (Russian chain of department stores acquired from Debenhams).

The division is focusing R&D on developing its next generation solution which contains in-memory processing – this feature should further differentiate TXT from its peers.

TXT Next

The division saw revenue growth of 33%, of which 6.5% was organic. Gross margin increased from 35.5% in FY15 to 42.7% in FY16, reflecting the higher software component within PACE. PACE has performed in line with expectations. The company is looking to combine the consultants from the original TXT Next services business with PACE's software business to offer a wider range of services to PACE's customer base. In 2016, the division signed new licence and service contracts with customers including Boeing (US), Pilatus (Switzerland), Reiser Simulation and Training (Germany), Goodrich Control Systems (UK) and Icelandair.

Outlook and changes to forecasts

We have made small changes to our FY17 revenue forecast reflecting the divisional split of revenues in FY16. We introduce a conservative 4% revenue growth rate for FY18 – successful cross-selling within TXT Next post the PACE acquisition could see this moving higher. The mix of software and services in TXT Next results in higher gross margins in FY17. This compensates for higher opex in FY17, as we increase our R&D and commercial cost forecasts. We leave our EBITDA forecast unchanged. A small reduction in depreciation and switching from net interest expense to net income boosts our PBT forecast. Overall, this results in a 7% increase in our normalised EPS forecast, although this remains marginally below the FY16 level. For FY18, we forecast 10% growth in normalised EPS. As the FY16 dividend was higher than expected, we have increased our FY17 and FY18 forecasts. The stronger end FY16 net cash position flows through to FY17 and increases further in FY18.

Exhibit 2: Changes to forecasts

	FY17e old	FY17e new	% change	% y-o-y	FY18e new	% y-o-y
Revenues (€m)	**74.7**	**74.9**	**0.3**	**8.3**	**77.9**	**4.1**
TXT Retail	39.0	39.0	-0.1	7.9	40.5	4.0
TXT Next	35.7	35.9	0.7	8.7	37.4	4.2
Gross margin (%)	53.3	54.2	0.8		54.1	0.0
Gross profit	39.8	40.6	1.8	9.3	42.2	4.0
EBITDA (€m)	**8.51**	**8.51**	**0.0**	**-2.4**	**9.37**	**10.1**
EBITDA margin (%)	11.4	11.4	0.0		12.0	0.7
Normalised EBIT (€m)	**7.7**	**7.9**	**2.0**	**-1.2**	**8.7**	**10.9**
Normalised EBIT margin (%)	10.3	10.5	0.2		11.2	0.7
Normalised net income (€m)	5.8	6.2	6.8	-2.8	6.9	10.8
Normalised EPS (€)	**0.50**	**0.53**	**7.1**	**-2.4**	**0.59**	**10.8**
Reported basic EPS (€)	0.42	0.46	8.4	-3.9	0.51	12.6
Net cash (€m)	**4.0**	**7.2**	**79.3**	**34.2**	**11.4**	**58.8**
Dividend (€)	0.27	0.32	18.5	6.7	0.33	3.1

Source: TXT e-solutions, Edison Investment Research

Exhibit 3: Financial summary

	€'000s	2012	2013	2014	2015	2016	2017e	2018e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		46,499	52,560	54,410	61,540	69,152	74,878	77,941
Cost of sales		(22,351)	(24,854)	(26,455)	(29,189)	(32,039)	(34,320)	(35,756)
Gross profit		24,148	27,706	27,955	32,351	37,113	40,558	42,185
EBITDA		5,322	6,263	5,324	6,659	8,715	8,508	9,365
Operating Profit (before amort and except)		4,283	5,241	4,284	5,820	7,955	7,858	8,715
Amortisation of acquired intangibles		0	(285)	(285)	(285)	(549)	(637)	(637)
Exceptionals and other income		939	0	1,468	0	(500)	0	0
Other income		0	0	0	(740)	0	(500)	(500)
Operating Profit		5,222	4,956	5,467	4,795	6,906	6,721	7,578
Net Interest		(37)	(435)	(249)	(151)	105	100	100
Profit Before Tax (norm)		4,246	4,806	4,035	5,669	8,060	7,958	8,815
Profit Before Tax (FRS 3)		5,185	4,521	5,218	4,644	7,011	6,821	7,678
Tax		(188)	121	(1,046)	(762)	(1,456)	(1,501)	(1,689)
Profit After Tax (norm)		4,092	4,927	3,226	4,739	6,386	6,207	6,876
Profit After Tax (FRS 3)		4,997	4,642	4,172	3,882	5,555	5,320	5,989
Average Number of Shares Outstanding (m)		11.0	11.5	11.5	11.7	11.7	11.7	11.7
EPS - normalised (c)		37	43	28	41	55	53	59
EPS - normalised fully diluted (c)		34	41	28	40	55	53	59
EPS - (IFRS) (c)		45	40	36	33	48	46	51
Dividend per share (c)		18.2	22.7	22.7	25.0	30.0	32.0	33.0
Gross margin (%)		51.9	52.7	51.4	52.6	53.7	54.2	54.1
EBITDA Margin (%)		11.4	11.9	9.8	10.8	12.6	11.4	12.0
Operating Margin (before GW and except) (%)		9.2	10.0	7.9	9.5	11.5	10.5	11.2
BALANCE SHEET								
Fixed Assets		18,570	17,850	18,019	18,132	25,428	24,761	24,094
Intangible Assets		16,621	15,370	15,078	14,692	21,296	20,629	19,962
Tangible Assets		1,154	1,118	1,249	1,361	1,598	1,598	1,598
Other		795	1,362	1,692	2,079	2,534	2,534	2,534
Current Assets		36,769	34,914	34,892	38,946	37,085	41,372	46,884
Stocks		1,388	1,451	1,820	2,075	3,146	3,246	3,346
Debtors		19,562	18,642	20,768	27,791	26,369	28,720	29,895
Cash		15,819	14,821	12,304	9,080	7,570	9,405	13,643
Other		0	0	0	0	0	0	0
Current Liabilities		(20,651)	(17,864)	(17,451)	(18,349)	(21,051)	(22,347)	(24,432)
Creditors		(15,155)	(14,512)	(15,297)	(17,528)	(20,243)	(21,539)	(23,624)
Short term borrowings		(5,496)	(3,352)	(2,154)	(821)	(808)	(808)	(808)
Long Term Liabilities		(8,666)	(6,965)	(6,491)	(5,105)	(7,180)	(7,180)	(7,180)
Long term borrowings		(4,301)	(2,896)	(1,685)	0	(1,391)	(1,391)	(1,391)
Other long term liabilities		(4,365)	(4,069)	(4,806)	(5,105)	(5,789)	(5,789)	(5,789)
Net Assets		26,022	27,935	28,969	33,624	34,282	36,606	39,367
CASH FLOW								
Operating Cash Flow		2,760	7,630	5,404	2,412	10,676	7,952	10,176
Net Interest		(37)	(435)	(249)	(151)	105	100	100
Tax		64	(1,615)	(1,344)	(1,461)	(2,022)	(1,501)	(1,689)
Capex		(405)	(483)	(615)	(763)	(738)	(620)	(620)
Acquisitions/disposals		(8,450)	19	0	0	(5,403)	(600)	0
Financing		1,690	(755)	(597)	2,215	(828)	0	0
Dividends		0	(2,107)	(2,615)	(2,678)	(2,931)	(3,496)	(3,729)
Net Cash Flow		(4,378)	2,254	(16)	(426)	(1,141)	1,836	4,238
Opening net debt/(cash)		(10,266)	(6,023)	(8,575)	(8,465)	(8,259)	(5,371)	(7,206)
HP finance leases initiated		0	0	0	0	0	0	0
Other		135	298	(94)	220	(1,747)	(0)	0
Closing net debt/(cash)		(6,023)	(8,575)	(8,465)	(8,259)	(5,371)	(7,206)	(11,444)

Source: TXT e-solutions, Edison Investment Research

Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
245 Park Avenue, 39th Floor
10167, New York
US

Sydney +61 (0)2 8249 8342
Level 12, Office 1205, 95 Pitt Street
Sydney NSW 2000
Australia