

TXT e-solutions

H121 results

Continuing on the M&A trail

TXT reported robust results for H121, with year-on-year organic revenue growth of 4.7% and recent fintech acquisitions adding a further 31.4% to growth; EBITDA margins expanded 0.4pp to 13.0% y-o-y. Since the end of H1, TXT has acquired a German internet of things (IoT) specialist for €10m, bolstering its exposure to the industrial sector and strengthening its operations in Germany. We estimate the deal is earnings accretive and raise our normalised EPS forecasts by 9% in FY21 and 13% in FY22.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/19	59.1	7.6	0.46	0.00	17.7	N/A
12/20	68.8	7.1	0.47	0.04	17.2	0.5
12/21e	90.9	9.5	0.58	0.06	13.8	0.7
12/22e	101.7	11.2	0.69	0.08	11.7	1.0

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

H121: Like-for-like revenue growth of 4.7%

TXT reported year-on-year revenue growth of 40% for Q221 and 36% for H121. Stripping out H220 acquisitions, like-for-like revenue grew 4.7% for H121. In Q221, the Aerospace & Aviation (A&A) division saw organic revenue growth of 19%, while Fintech grew 81% y-o-y, but saw a 7% decline on an organic basis. Group EBITDA increased 42.5% y-o-y in Q221 and 40.1% in H121, with margin expansion in both periods. Net cash at the end of H121 stood at €11.1m.

M&A focus switches to A&A division

In August, TXT acquired TeraTron, a German specialist in IoT solutions used in the automotive, industrial and healthcare sectors. This business will sit within the A&A division, roughly doubling the contribution to this division from the industrial and automotive segment. At a price of €10m, the deal was valued at a price multiple of 1.1x FY21e revenue and 5.1x FY21e EBITDA, versus 1.1x and 8.9x respectively for TXT (based on pre-deal forecasts). We have revised our forecasts to reflect this accretive deal, raising normalised diluted EPS forecasts by 9% in FY21 and 13% in FY22. Management indicated that it expects to make further acquisitions and is willing to use debt to do so.

Valuation: At a discount

TXT continues to trade at a discount to its peer group on all measures, despite the deployment of a large proportion of the company's cash balance into acquisitions, and revenue growth and profitability above the group average. Evidence of improving demand from civil aviation in the A&A division and the banking sector within the Fintech division, growing revenues from the earlier stage fintech businesses and successful integration of TeraTron should help to reduce this discount.

Software & comp services

9 August 2021

Price €8.06

Market cap €94m

\$1.19/€

Net cash (€m) at end H121 11.1

Shares in issue 11.7m

Free float 50.0%

Code TXT

Primary exchange Borsa Italiana (STAR)

Secondary exchange N/A

Share price performance



Business description

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

Next events

Q321 results 8 November

Analyst

Katherine Thompson +44 (0)20 3077 5730

tech@edisongroup.com
[Edison profile page](#)

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Review of H121 results

Exhibit 1: Q221 and H121 results highlights

€m	Q221	Q220	y-o-y	H121	H120	y-o-y
Revenues	22.2	15.9	40.1%	43.7	32.1	36.1%
Gross profit	8.3	6.7	23.7%	16.6	14.0	18.5%
Gross margin	37.6%	42.6%	-5.0%	38.0%	43.7%	-5.6%
EBITDA	3.0	2.1	42.5%	5.7	4.0	40.1%
EBITDA margin	13.3%	13.1%	0.2%	13.0%	12.6%	0.4%
Normalised EBIT	2.4	1.6	53.2%	4.6	3.1	48.3%
Normalised EBIT margin	11.0%	10.0%	0.9%	10.6%	9.7%	0.9%
Reported EBIT	1.7	0.9	82.0%	3.4	2.1	62.7%
Reported EBIT margin	7.6%	5.9%	1.8%	7.8%	6.5%	1.3%
Reported net income	0.8	2.5	-66.4%	2.1	2.7	-24.1%
Net cash	11.1	38.3	-70.9%	11.1	38.3	-70.9%

Source: TXT e-solutions

TXT reported year-on-year revenue growth of 40.1% for Q221 and 36.1% for H121. As MAC Solutions and HSPI were acquired in H220, stripping them out results in like-for-like revenue growth of 4.7% for H121. The gross margin reduced by 5.0pp for Q221 and 5.6pp for H121 for a couple of reasons: the two acquisitions in H220 were for services businesses, which typically have lower margins than those selling software; and within the A&A division, certain R&D staff worked on customisation projects for specific customers in Q221 so their costs were allocated to cost of sales rather than opex. EBITDA increased 42.5% y-o-y in Q221 and 40.1% in H121, with margin expansion in both periods. Normalised operating profitability also improved year-on-year. Reported net income in Q220 and H120 benefited from a lower-than-normal tax rate and financial income relating to the cash invested in short-term securities, hence the decline in reported net income in both Q221 and H121. Net cash has declined from the end of FY20, when it stood at €22.1m, but is up marginally from the €10.8m reported at the end of Q121. In Q121, the company paid for the 9% stake in Banca del Fucino (€14.3m) and the minority interest in Assiipay (€0.9m).

Divisional performance

Exhibit 2 shows the performance of TXT's two divisions for both Q2 and H121.

Exhibit 2: Divisional revenue performance

Revenues (€m)	Q221	Q220	y-o-y	H121	H120	y-o-y
Aerospace & Aviation (A&A)	12.3	10.3	19.3%	23.3	20.9	11.8%
Software licences & maintenance	1.9	1.8	5.1%	3.5	3.8	-6.5%
Services	10.4	8.5	22.4%	19.8	17.1	15.8%
EBITDA				3.2	2.9	11.9%
EBITDA margin				13.7%	13.7%	0.0%
Fintech	9.9	5.5	79.0%	20.4	11.2	81.2%
Software licences & maintenance	0.4	0.3	12.7%	0.7	0.6	11.3%
Services	9.5	5.2	83.0%	19.7	10.6	85.3%
EBITDA				2.5	1.2	107.8%
EBITDA margin				12.1%	10.6%	1.5%
Total software licences & maintenance	2.3	2.1	6.2%	4.2	4.4	-4.0%
Total services	20.0	13.7	45.4%	39.5	27.7	42.4%

Source: TXT e-solutions

Aerospace & Aviation: 19% organic growth in Q221

The A&A division saw revenue growth of 19.3% y-o-y for Q221 and 11.8% for H121. The majority of new business is currently from the defence sector, but the business is seeing the beginnings of an increase in demand from the civil aviation sector.

During H1, notable contracts included:

- **FlyZero project:** PACE will supply licences for its preliminary aircraft and systems design suite and its route and aircraft economic analysis tool to the Aerospace Technology Institute's (ATI) FlyZero Project. The project, led by ATI and backed by the UK government, is investigating the design challenges, manufacturing requirements and market opportunities of zero-carbon emission aircraft.
- **Drone JV:** TXT, Politecnico di Milano and ANT-X are collaborating to develop and test innovative solutions and services based on the use of drones in conjunction with helicopters to be used in rescue missions.

The EBITDA margin of 13.7% was flat year-on-year.

Fintech: Acquisitions drive H121 growth of 81%

The Fintech division saw year-on-year revenue growth of 79.0% in Q221 and 81.2% in H121. We estimate that MAC Solutions and HSPI contributed revenue of €10m; excluding this, the division saw a revenue decline of 7% y-o-y in H121. The division's EBITDA margin expanded from 10.6% in H120 to 12.1% in H121, helped by the recent acquisitions. TXT Working Capital Solutions and TXT Risk Solutions, both start-up businesses, are still loss-making, contributing a loss of €0.75m to EBITDA in H121. The company expects the former to reach break-even in FY22 and the latter this year.

Notable contracts in H121 included:

- **Polaris new financial partner:** Polaris, from TXT Working Capital Solutions, helps provide supply chain finance to companies. For the platform to be successful it will need to connect providers of finance with those that require it. Banca UBAE has joined Polaris as a financial partner.
- **INAIL contract:** HSPI has won a contract, as part of a consortium that includes Il Sole 24 Ore, to manage INAIL's editorial web publishing and media relations support services.

M&A update

TeraTron acquisition bolsters industrial segment within A&A

On 1 August, the company completed the acquisition of 100% of TeraTron. TeraTron is a German designer and developer of innovative IoT solutions for digitalisation, automation and security, with a focus on the automotive, industrial (Industry 4.0) and healthcare markets and a growing presence in other innovative and high-tech sectors. TeraTron's international customer base includes Audi, BMW, HILTI, John Deere, Porsche, Volkswagen and Volvo. TeraTron provides an end-to-end offering, from identification of customer needs and design to production, maintenance and after-sales support, with expertise in technologies such as radio-frequency identification (RFID), transponders, near field communication (NFC), Bluetooth, wireless local area network (WLAN), encoding/cryptology, vehicle interfaces (CAN/LIN: controller area network/local interconnect network) and iOS/Android apps. TeraTron produces its own hardware for use in these solutions, integrated with proprietary software.

The table below shows historical and expected financial performance over three years, with COVID-19 clearly having an impact on performance in FY20. TXT has paid €10.1m in cash for the

business, which will sit within the A&A division. This should boost the company's exposure to the manufacturing sector. For H121, TXT disclosed that the industrial, manufacturing, automotive and transportation sectors made up 14% of A&A revenue and 7% of group revenue.

Exhibit 3: TeraTron financial and valuation data

€m	FY19	FY20	FY21e
Revenue	9.2	7.6	9.0
EBITDA	1.8	1.4	2.0
EBITDA margin	20%	18%	22%
Revenue growth		-17%	18%
Price/sales	1.1	1.3	1.1
Price/EBITDA	5.6	7.2	5.1

Source: TXT e-solutions

Investment in wealth management solutions business

In Q2, TXT invested in a start-up called ReVersal SpA, obtaining a 51% stake for a cash payment of €0.51m. ReVersal is developing wealth management solutions; TXT expects this to be break-even in the first year of operation.

More M&A planned

Management confirmed that it continues to consider acquisitions to grow the business. While most of the cash that was left after the sale of TXT Retail has been spent, the company confirmed that it would consider using debt up to a limit of 2x EBITDA. It also has 1.3m treasury shares that could be used for acquisitions.

Outlook and changes to forecasts

The company expects to be able to maintain the EBITDA margin at a similar rate in H221. We have revised our forecasts to reflect H121 results as well as the recent TeraTron acquisition. We note that TeraTron generates EBITDA margins in excess of TXT's H121 margin of 13%.

Exhibit 4: Changes to forecasts

	FY21e old	FY21e new	change	y-o-y	FY22e old	FY22e new	change	y-o-y
Revenues (€m)	86.7	90.9	4.8%	32.3%	92.4	101.7	10.1%	11.9%
Gross margin	40.8%	39.4%	(1.4%)	(3.2%)	41.6%	42.0%	0.3%	2.5%
Gross profit	35.4	35.8	1.2%	22.4%	38.5	42.7	10.9%	19.1%
EBITDA (€m)	10.89	11.82	8.5%	38.1%	12.17	13.73	12.9%	16.2%
EBITDA margin	12.6%	13.0%	0.4%	0.5%	13.2%	13.5%	0.3%	0.5%
Normalised EBIT (€m)	8.80	9.60	9.1%	46.7%	10.07	11.32	12.4%	18.0%
Normalised EBIT margin	10.1%	10.6%	0.4%	1.0%	10.9%	11.1%	0.2%	0.6%
Reported operating profit (€m)	6.9	7.4	7.1%	128.0%	8.2	9.4	15.3%	27.6%
Normalised net income (€m)	6.3	6.8	9.3%	24.9%	7.2	8.1	12.6%	18.1%
Reported net income (€m)	4.9	5.2	7.2%	15.1%	5.8	6.7	15.5%	28.0%
Normalised diluted EPS (€)	0.53	0.58	9.3%	24.5%	0.61	0.69	12.7%	18.0%
Reported basic EPS (€)	0.42	0.45	7.3%	14.8%	0.50	0.57	15.7%	27.9%
Net cash (€m)	13.6	2.4	(82.3%)	(89.1%)	20.3	9.0	(55.7%)	272.8%
Dividend (€)	0.06	0.06	0.0%	50.0%	0.08	0.08	0.0%	33.3%

Source: Edison Investment Research

Valuation

The table below shows TXT's valuation versus its peer group of European software and services providers. TXT continues to trade at a discount to its peer group on all measures, despite the deployment of a large proportion of the company's cash balance into acquisitions, and revenue

growth and profitability above the group average. In our view, the company's exposure to the aerospace and aviation market is likely to be weighing on the share price, as is uncertainty over the likely performance of the recent spate of acquisitions. We expect this discount to reduce as TXT provides evidence of:

- A&A: performance remaining stable at least, until customers in COVID-19-hit sectors, particularly civil aviation, feel more confident of their futures and resume/accelerate orders; successful integration of the TeraTron acquisition.
- Fintech: the early-stage businesses (TXT Risk Solutions, TXT Working Capital Solutions) starting to generate material revenues and reaching break-even; banks resuming normal activity for software testing; international revenues growing.
- Overall, software revenues growing as a percentage of the total, as these generate much higher gross margins.

Exhibit 5: Peer financial and valuation metrics

Company	Share price	Market cap	Rev growth		EBIT margin		EBITDA margin		EV/sales		EV/EBIT		P/E		Div yield	
	€	€m	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY
TXT	8.06	94	32.3%	11.9%	10.6%	11.1%	13.0%	13.5%	0.8	0.7	7.5	6.4	13.8	11.7	0.7%	1.0%
European IT services companies																
AKKA Technologies	47.00	1,467	2.8%	7.0%	0.4%	6.2%	10.5%	10.2%	1.2	1.1	272.0	17.6	N/A	23.7	0.0%	0.6%
Alten	137.10	4,709	16.7%	8.5%	7.9%	8.8%	10.9%	11.6%	1.7	1.6	21.7	17.9	27.9	24.3	0.8%	0.8%
AtoS	39.09	4,301	-1.1%	1.1%	5.4%	5.9%	11.1%	12.0%	0.6	0.6	11.3	10.2	9.3	7.3	2.5%	2.6%
Cap Gemini	189.50	31,993	11.1%	6.9%	11.6%	12.1%	15.5%	15.7%	2.1	2.0	18.5	16.5	23.3	21.0	1.1%	1.2%
Devoteam	134.00	1,117	4.7%	6.6%	10.0%	10.3%	12.0%	12.0%	1.3	1.2	13.2	12.0	24.0	21.6	0.9%	1.0%
ESI Group	60.80	362	5.7%	6.2%	4.9%	6.0%	9.6%	11.3%	2.9	2.7	59.1	45.4	95.0	68.0	0.8%	1.0%
Reply	154.50	5,782	16.6%	11.2%	13.6%	13.8%	16.4%	16.3%	3.9	3.5	28.4	25.1	41.1	36.6	0.4%	0.5%
Sopra Steria	169.60	3,484	8.6%	4.5%	7.1%	7.8%	11.3%	12.0%	0.9	0.9	13.0	11.3	16.2	13.6	1.6%	1.6%
Average			8.1%	6.5%	7.6%	8.9%	12.2%	12.6%	1.8	1.7	54.7	19.5	33.8	27.0	1.0%	1.2%
(Discount)/premium to peers									(57%)	(58%)	(86%)	(67%)	(59%)	(57%)	(26%)	(14%)

Source: Edison Investment Research, Refinitiv (as at 6 August)

Exhibit 6: Financial summary

	€'000s	2016	2017	2018	2019	2020	2021e	2022e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		33,060	35,852	39,957	59,091	68,753	90,932	101,726
Cost of sales		(18,954)	(20,224)	(22,289)	(31,825)	(39,469)	(55,100)	(59,050)
Gross profit		14,106	15,628	17,668	27,266	29,284	35,832	42,676
EBITDA		4,260	3,536	4,098	7,004	8,560	11,820	13,731
Operating Profit (before amort and except)		3,954	3,180	2,755	5,408	6,542	9,600	11,323
Amortisation of acquired intangibles		(264)	(439)	(610)	(1,142)	(1,340)	(1,900)	(1,900)
Exceptionals and other income		(557)	0	(300)	(713)	(1,963)	(316)	0
Other income		0	(69)	0	0	0	0	0
Operating Profit		3,133	2,672	1,845	3,553	3,239	7,384	9,423
Net Interest		48	(208)	(1,284)	2,194	562	(100)	(100)
Profit Before Tax (norm)		4,002	2,972	1,471	7,602	7,104	9,500	11,223
Profit Before Tax (FRS 3)		3,181	2,464	561	2,315	5,958	7,284	9,323
Tax		(661)	(710)	4	(1,867)	(1,162)	(2,040)	(2,611)
Profit After Tax (norm)		3,170	2,170	1,204	5,473	5,718	6,840	8,081
Profit After Tax (FRS 3)		2,520	1,754	565	448	4,796	5,245	6,713
Ave. Number of Shares Outstanding (m)		11.7	11.7	11.7	11.7	11.7	11.7	11.7
EPS - normalised (€)		0.271	0.186	0.102	0.456	0.470	0.585	0.690
EPS - normalised fully diluted (€)		0.271	0.186	0.102	0.456	0.470	0.585	0.690
EPS - (IFRS) (€)		0.475	5.874	0.048	0.027	0.391	0.448	0.574
Dividend per share (€)		0.30	1.00	0.50	0.00	0.04	0.06	0.08
Gross margin (%)		42.7	43.6	44.2	46.1	42.6	39.4	42.0
EBITDA Margin (%)		12.9	9.9	10.3	11.9	12.5	13.0	13.5
Operating Margin (before GW and except) (%)		12.0	8.9	6.9	9.2	9.5	10.6	11.1
BALANCE SHEET								
Fixed Assets		25,428	8,860	22,942	34,635	47,411	70,701	67,293
Intangible Assets		21,296	7,332	17,751	24,380	37,652	47,896	45,880
Tangible Assets		1,598	793	3,680	7,929	7,460	6,206	4,814
Other		2,534	735	1,511	2,326	2,299	16,599	16,599
Current Assets		37,085	109,426	134,674	127,052	126,036	106,822	111,120
Stocks		3,146	2,528	3,141	4,156	4,749	5,049	5,349
Debtors		26,369	17,215	16,992	24,150	41,193	49,826	55,740
Cash		7,570	89,683	114,541	98,746	80,094	51,947	50,031
Other		0	0	0	0	0	0	0
Current Liabilities		(21,051)	(13,612)	(29,366)	(43,129)	(55,446)	(62,391)	(65,771)
Creditors		(20,243)	(12,937)	(12,062)	(17,823)	(24,811)	(31,756)	(35,136)
Short term borrowings		(808)	(675)	(17,304)	(25,306)	(30,635)	(30,635)	(30,635)
Long Term Liabilities		(7,180)	(4,781)	(41,903)	(36,538)	(32,138)	(23,638)	(15,138)
Long term borrowings		(1,391)	(1,688)	(36,882)	(32,029)	(27,398)	(18,898)	(10,398)
Other long term liabilities		(5,789)	(3,093)	(5,021)	(4,509)	(4,740)	(4,740)	(4,740)
Net Assets		34,282	99,893	86,347	82,020	85,863	91,494	97,505
CASH FLOW								
Operating Cash Flow		10,676	119	2,039	(354)	1,244	9,516	10,897
Net Interest		105	(208)	(69)	3,102	(988)	(100)	(100)
Tax		(2,022)	379	(624)	(229)	(1,332)	(2,040)	(2,611)
Capex		(738)	(661)	(548)	(916)	(1,156)	(850)	(900)
Acquisitions/disposals		(5,403)	82,250	1,314	(2,178)	(11,701)	(25,575)	0
Financing		(828)	(6)	(7,208)	(4,287)	(2,648)	(130)	0
Dividends		(2,931)	(3,496)	(11,710)	(5,781)	0	(468)	(702)
Net Cash Flow		(1,141)	78,377	(16,806)	(10,643)	(16,581)	(19,647)	6,584
Opening net debt/(cash)		(8,259)	(5,371)	(87,320)	(60,355)	(41,412)	(22,061)	(2,414)
HP finance leases initiated		0	0	(2,788)	(2,500)	0	0	0
Other		(1,747)	3,572	(7,371)	(5,800)	(2,770)	0	(0)
Closing net debt/(cash)		(5,371)	(87,320)	(60,355)	(41,412)	(22,061)	(2,414)	(8,998)

Source: TXT e-solutions, Edison Investment Research

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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
1185 Avenue of the Americas
3rd Floor, New York, NY 10036
United States of America

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia
