

S&T

Germany | IT software & services | MCAP EUR 240.3m

23 December 2015

Buy (Buy)

Target Price EUR 6.70
Current Price EUR 5.5
Up/downside 21.0%
Change in TP 19.64%
Change in EPS 2.1% 2015E

Equity story yet to unfold

Although S&T's discount to peers has reduced as a result of the shares' appreciation (+20% in, +75% YTD), our conviction remains bullish. We argue that the equity story has far from delivered its full potential. Buy, TP raised from EUR5.60 to EUR6.70.

Good visibility ahead, TP raised from EUR5.60 to EUR6.70

We raise our top-line growth estimates for 2016 (c. 3% change) to take into account a robust order backlog (EUR198m after 9M 2015, +26% YOY, +15% QOQ) and bullish guidance for 2016 ("double-digit sales growth and profits rising even faster than that"), a sign of management's high optimism. In the near term, IT security appliances, S&T's "cash cow", and Services in eastern Europe ("Services EE") should drive earnings up (KECH 2015E:+11% in EPS 2015E), supported by increasing needs in the Internet of Things (e.g. protection of welding robots) and solid demand for IT services in eastern Europe, mainly Poland and Romania.

"Smart Grid" ramp-up on track

In line with the group's target, we expect the smart grid business to turn profitable in 2016 (vs. net loss of EUR2m this year, due to start-up costs), with organic growth also taking off (+30%). S&T seems well set up to tackle a market worth EUR25bn (estimated investments in CEE for smart grid infrastructure roll-out by 2025). Via NES, its dedicated subsidiary, S&T has structured a commercial offering around new and greater-margin products (launch of Patagonia platform) while refocusing entirely on the core European region. We expect a share of the current project pipeline (hundreds of millions) to convert into sales as of 2016. The most promising project at the moment is the plan for the roll-out of 5m smart meters to cover southern Poland (order value of >USD500m). We note that NES is part of the ongoing pilot project in the city of Wroclaw and is therefore well positioned to take part of it.

Benefits from shift in business model still to come

S&T's value-oriented strategy (transformation into a technology company) has yet to be translated into numbers, but we believe it could be highly rewarding. Thanks to relatively inexpensive and well-targeted acquisitions, S&T has captured a valuable position in promising growth markets and is now ideally positioned to leverage its large customer base in eastern Europe through the sale of higher-margin IT solutions. The investment case combines solid growth prospects (including potential game-changing deal opportunities) and a strong case for value creation (product-mix improvement, scaling back of unprofitable businesses). Currently trading at 11x earnings for 2017E, the potential is not fairly priced, in our view. Buy, new TP of EUR6.70.

Baptiste de Leudeville

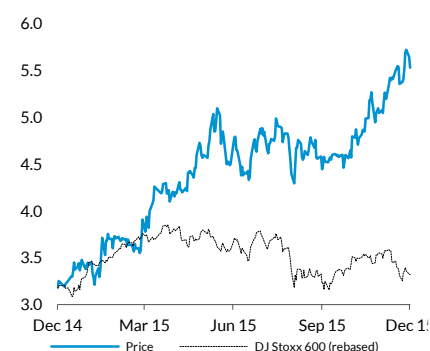
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Market data

Bloomberg: SANT GR	Reuters: SANT1.DE
Market cap (EURm)	240
Free float	66%
No. of shares outstanding (m)	43
Avg. daily volume('000)	38
YTD abs performance	71.9%
52-week high/low (EUR)	5.73/3.19

FY to 31/12 (EUR)	12/15E	12/16E	12/17E
Sales (m)	465.6	519.3	560.7
EBITDA adj (m)	26.0	33.5	38.2
EBIT adj (m)	18.6	25.2	29.3
Net profit adj (m)	15.3	18.9	22.2
Net fin. debt (m)	-5.2	-18.7	-36.9
FCF (m)	10.0	18.8	24.1
EPS adj. and fully dil.	0.35	0.43	0.50
Consensus EPS	0.33	0.41	0.48
Net dividend	0.07	0.09	0.10

FY to 31/12 (EUR)	12/15E	12/16E	12/17E
P/E adj and ful. dil.	15.9	12.9	11.0
EV/EBITDA	9.1	6.7	5.4
EV/EBIT	12.8	8.9	7.0
FCF yield	4.2%	7.8%	10.0%
Dividend yield	1.3%	1.6%	1.8%
Net fin.debt/EBITDA	-0.2	-0.6	-1.0
Gearing	-5.0%	-15.2%	-25.1%
ROIC	14.7%	18.4%	-6.8%
EV/IC	2.4	2.1	1.9



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Valuation update: TP raised from EUR5.60 to EUR6.70

DCF

We discount future cash flows using a 10% WACC and a perpetuity growth rate of 1.5%

Table 1: WACC summary

Pretax cost of debt	5.2%
Marginal tax rate	25.0%
After tax cost of debt	3.9%
Risk-free rate (Rf)	2.0%
Market Return (Rm)	7.5%
Market premium (Rm-Rf)	5.5%
Beta	2.00
Cost of Equity	13.0%
Debt (% of EV)	33%
Equity (% of EV)	67%
WACC	10.0%
Terminal growth	1.5%

Source: Kepler Cheuvreux

We expect a revenue CAGR of 5.7% in 2015-20, mainly supported by Appliances in Smart Grid (+16%) and IT security (+9%). We factor in an even higher progression of EBITDA (+13%) during the same period. Investments in smart grids will be concentrated over the next three years. This valuation derives a fair value of **EUR7.4** per share.

Table 2: DCF summary

EURm	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2025+
Sales	519.3	560.7	597.7	627.1	651.1	669.2	686.0	701.1	714.4	725.6	736.5
growth	20.8%	11.5%	8.0%	6.6%	4.9%	3.8%	2.8%	2.5%	2.2%	1.9%	1.5%
EBITDA	33.5	38.2	43.0	48.4	54.0	57.5	61.2	62.7	64.0	65.1	58.9
EBITDA margin	5.6%	6.5%	6.8%	7.2%	7.7%	8.3%	8.6%	8.9%	8.9%	9.0%	8.0%
EBIT	25.2	29.3	33.5	38.4	43.6	46.8	50.2	51.5	52.5	53.4	47.9
EBIT margin	4.0%	4.9%	5.2%	5.6%	6.1%	6.7%	7.0%	7.3%	7.3%	7.4%	6.5%
NOPAT	20.2	23.4	26.8	30.7	34.9	37.4	40.2	41.2	42.0	42.8	38.3
add back D&A	8.3	9.0	9.6	10.0	10.4	10.7	11.0	11.2	11.4	11.6	11.8
% of sales	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%	-1.6%
WCR	36.4	39.2	41.8	43.9	45.6	46.8	48.0	49.1	50.0	50.8	51.6
% of revenues	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%
Change in WC	-3.8	-2.9	-2.6	-2.1	-1.7	-1.3	-1.2	-1.1	-0.9	-0.8	-0.8
Capital expenditures	-10.9	-11.2	-11.4	-11.3	-11.7	-11.4	-11.7	-11.9	-12.1	-12.3	-12.5
% of sales	2.1%	2.0%	1.9%	1.8%	1.8%	1.7%	1.7%	1.7%	1.7%	1.7%	1.7%
Free cash flow	13.8	18.3	22.4	27.4	31.9	35.5	38.3	39.4	40.4	41.3	36.8
% of sales	2.7%	3.3%	3.7%	4.4%	4.9%	5.3%	5.6%	5.6%	5.7%	5.7%	5.0%
Discounted FCF	12.6	15.1	16.8	18.7	19.8	20.0	19.7	18.4	17.1	15.9	
Sum of discounted FCF	174.1										
Terminal Value	167.1										
Value of operations	341.2										
Cash	36.2										
Debt	54.3										
Minorities	2.8										
Equity Value	320.3										
Equity value per share	7.4										

Source: Kepler Cheuvreux

In parallel, we conduct a sensitivity analysis on our DCF, which provides a valuation range of EUR6.3 to EUR8.9 per share.

Table 3: Sensitivity analysis

		Perpetual growth					LT EBIT margin		
		1.0%	1.5%	2.0%			6.0%	6.5%	7.0%
WACC	11.0%	6.3	6.5	6.6	WACC	11.0%	6.2	6.5	6.7
	10.5%	6.7	6.9	7.1		10.5%	6.6	6.9	7.2
	10.0%	7.2	7.4	7.6		10.0%	7.1	7.4	7.7
	9.5%	8.7	7.9	8.2		9.5%	7.6	7.9	8.3
	9.0%	8.3	8.5	8.9		9.0%	8.1	8.5	8.9

Source: xxx

Peers

Based on a set of forward valuation multiples for 2016 and 2017, S&T is trading at a 7% average discount to peers. The sharp appreciation of the shares since our last company report (+54% since March 2015) allowed a good part of the valuation gap with S&T's closest competitors to be closed.

Our peer sample selection is composed of similarly sized IT companies active in Central and eastern Europe.

Allgeier (market cap EUR147m) is a Germany-based company operating in the IT services sector. The company provides IT infrastructure and software services, consulting related to cloud computing, security, ECM and ERP. Around 80% of its revenues are generated in Germany.

Bechtle (market cap EUR1,805m) is a German IT company whose business model combines IT sales (e-commerce segment) and system house services (IT service providing). It is mostly active throughout the DACH region, where it supplies IT applications to small and medium-sized companies, large corporate groups, financial service providers and public institutions.

Cancom (market cap EUR624m) is one of the leading suppliers of IT infrastructure and professional services in Germany and Austria. Cancom has transformed from a pure supplier of hardware and software products into an important integrated IT services provider and cloud business. The group has a turnover of over EUR800m.

Table 4: Peers sample operating performance - consensus

EBIT margin	2015E	2016E	2017E
Allgeier	3.3%	4.4%	5.3%
Bechtle	4.4%	4.6%	4.7%
Cancom	4.3%	5.2%	5.7%
S&T (KECH)	4.0%	4.9%	5.2%

Source: Thonsom Reuters, Kepler Cheuvreux

Table 5: Peer sample revenue growth - consensus

Revenue growth	2015E	2016E	2017E
Allgeier	11.3%	8.6%	12.2%
Bechtle	6.8%	6.6%	8.5%
Cancom	9.7%	7.3%	7.2%
S&T (KECH)	20.8%	11.5%	8.0%

Source: Kepler Cheuvreux

 This method derives a value of **EUR6.1 per share**.

Table 6: Peer multiples

	EV/sales		EV/EBITDA		EV/EBIT		P/E	
	2016E	2017E	2016E	2017E	2016E	2017E	2016E	2017E
Allgeier	0.4	0.4	6.6	5.6	9.9	7.6	12.0	8.7
Cancom	0.6	0.6	8.5	7.6	11.7	10.0	19.0	15.7
Bechtle	0.5	0.5	10.7	9.8	12.7	11.5	14.6	12.6
Average	0.52	0.49	8.6	7.6	11.4	9.7	15.2	12.3
S&T	0.52	0.48	7.9	6.8	10.5	8.8	12.5	10.7
Premium/Discount	-0.7%	-1.5%	-7.7%	-10.8%	-7.8%	-9.1%	-17.9%	-13.1%

Source: Kepler Cheuvreux

Estimates breakdown

Table 7: Sales estimates

EURm	2014A	2015E	2016E	2017E	2018E	2019E	2020E
Services EE	217.2	260.6	286.7	298.2	307.1	314.8	321.1
Growth	8.8%	20.0%	10.0%	4.0%	3.0%	2.5%	2.0%
Services DACH	89.6	75.3	71.5	70.1	70.1	70.1	70.1
Growth	-7.3%	-16.0%	-5.0%	-2.0%	0.0%	0.0%	0.0%
Appliances Security	50.0	75.0	90.0	103.5	113.9	119.5	124.9
Growth	20.2%	50.0%	20.0%	15.0%	10.0%	5.0%	4.5%
Appliances Smart Grid	28.8	54.7	71.1	88.9	106.7	122.7	135.0
Growth	NA	90.0%	30.0%	25.0%	20.0%	15.0%	10.0%
Total	385.6	465.6	519.3	560.7	597.7	627.1	651.1
Growth	14.1%	20.8%	11.5%	8.0%	6.6%	4.9%	3.8%

Source: Kepler Cheuvreux

Table 8: EBITDA estimates

EURm	2014A	2015E	2016E	2017E	2018E	2019E	2020E
EBITDA	22.9	26.0	33.5	38.2	43.0	48.4	54.0
<i>Growth</i>	14.0%	13.7%	28.7%	14.1%	12.5%	12.6%	11.5%
<i>EBITDA margin</i>	5.9%	5.6%	6.5%	6.8%	7.2%	7.7%	8.3%
Services EE	10.8	10.4	12.2	13.4	13.8	15.0	16.1
<i>Growth</i>	33.7%	-3.1%	16.9%	10.1%	3.0%	8.2%	7.4%
<i>EBITDA margin</i>	5.0%	4.0%	4.3%	4.5%	4.5%	4.8%	5.0%
Services DACH	1.1	3.2	3.2	3.2	3.2	3.3	3.5
<i>Growth</i>	-42.3%	194.0%	0.6%	-2.0%	0.0%	5.6%	5.3%
<i>EBITDA margin</i>	1.2%	4.3%	4.5%	4.5%	4.5%	4.8%	5.0%
Appliances Security	8.6	13.5	16.0	18.1	19.6	20.3	20.9
<i>Growth</i>	-14.7%	56.1%	18.3%	13.4%	8.4%	3.5%	3.0%
<i>EBITDA margin</i>	17.3%	18.0%	17.8%	17.5%	17.3%	17.0%	16.8%
Appliances Smart Grid	2.4	-1.1	2.1	3.6	6.4	9.8	13.5
<i>Growth</i>	NA	-145.9%	-295.0%	66.7%	80.0%	53.3%	37.5%
<i>EBITDA margin</i>	1067.4%	-2.0%	3.0%	4.0%	6.0%	8.0%	10.0%

Source: Kepler Cheuvreux

Key financials

FY to 31/12 (EUR)	2010	2011	2012	2013	2014	2015E	2016E	2017E
Per share data								
EPS adjusted	0.19	0.29	0.26	0.30	0.32	0.35	0.44	0.51
EPS adj and fully diluted	0.19	0.29	0.26	0.30	0.32	0.35	0.43	0.50
EPS reported	0.19	0.29	0.26	0.30	0.32	0.35	0.44	0.51
Cash flow per share	-0.16	0.06	0.43	0.28	0.50	0.47	0.69	0.81
Book value per share	1.67	2.09	2.16	1.76	2.12	2.32	2.78	3.32
Dividend per share	0.00	0.00	0.00	0.06	0.06	0.07	0.09	0.10
Number of shares, YE (m)	19.63	23.54	28.28	39.20	41.00	43.41	43.41	43.41
Valuation								
P/E adjusted	11.4	8.2	8.9	7.9	9.0	15.7	12.7	10.8
P/E adjusted and fully diluted	11.4	8.2	8.9	7.9	9.0	15.9	12.9	11.0
P/BV	1.3	1.1	1.1	1.4	1.3	2.4	2.0	1.7
P/CF	na	39.5	5.3	8.4	5.7	11.9	8.1	6.8
Dividend yield (%)	0.0%	0.0%	0.0%	2.5%	2.1%	1.3%	1.6%	1.8%
FCF yield (%)	-9.7%	-2.5%	14.0%	5.7%	12.7%	4.2%	7.8%	10.0%
EV/Sales	0.5	0.6	0.2	0.3	0.3	0.5	0.4	0.4
EV/EBITDA	8.2	7.0	5.0	5.2	5.3	9.1	6.7	5.4
EV/EBIT	11.6	9.0	7.4	7.3	7.3	12.8	8.9	7.0
Income Statement (EURm)								
Sales	80.7	153.2	339.5	338.0	385.6	465.6	519.3	560.7
EBITDA adjusted	4.5	12.2	16.6	20.1	22.9	26.0	33.5	38.2
EBIT adjusted	3.2	9.5	11.1	14.4	16.7	18.6	25.2	29.3
Net financial items & associates	-0.4	-1.0	-1.4	-2.2	-1.8	-1.6	-1.6	-1.6
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tax	1.2	-0.3	-0.3	-0.1	-0.8	-1.7	-4.7	-5.5
Net profit from continuing operations	4.0	8.1	9.4	12.0	14.1	15.3	18.9	22.2
Net profit from discontinuing activities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit before minorities	4.0	8.1	9.4	12.0	14.1	15.3	18.9	22.2
Net profit reported	3.7	6.9	7.3	11.8	13.0	15.3	18.9	22.2
Net profit adjusted	3.7	6.9	7.3	11.8	13.0	15.3	18.9	22.2
Cash Flow Statement (EURm)								
Cash flow from operating activities	-3.1	1.4	12.3	11.2	20.6	20.3	29.8	35.3
Capex	-1.0	-2.8	-3.2	-5.8	-5.8	-10.2	-10.9	-11.2
Free cash flow	-4.1	-1.4	9.1	5.4	14.9	10.0	18.8	24.1
Acquisitions & Divestments	-1.2	-11.6	0.4	5.5	-2.9	0.0	0.0	0.0
Dividend paid	0.0	-0.1	-0.3	-0.3	-3.8	-3.1	-3.8	-4.4
Others	3.7	1.4	0.0	-3.1	7.7	-0.3	-1.6	-1.6
Change in net financial debt	-1.6	-11.6	9.3	7.4	15.9	6.7	13.5	18.1
Balance Sheet (EURm)								
Intangible assets	20.6	40.9	38.8	44.8	57.1	58.5	59.8	60.9
Tangible assets	2.7	11.1	9.9	9.0	11.4	12.8	14.1	15.3
Financial & other non-current assets	3.0	13.6	13.7	13.9	17.4	16.1	16.1	16.1
Total shareholders' equity	33.4	54.6	63.1	71.2	89.7	103.7	123.5	146.8
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities and provisions	31.5	172.5	150.0	148.9	183.3	219.0	235.9	249.0
Net debt	-5.7	23.6	14.9	9.3	1.5	-5.2	-18.7	-36.9
Working capital requirement	6.1	23.2	24.3	23.9	22.3	28.0	31.8	34.7
Invested Capital	29.4	75.2	73.1	77.6	90.8	99.4	105.7	110.9
Ratios								
ROE (%)	14.5%	16.7%	13.2%	18.1%	16.7%	16.3%	17.1%	16.7%
ROIC (%)	12.8%	13.6%	11.3%	14.3%	14.8%	14.7%	18.4%	-6.8%
Net fin. debt / EBITDA (x)	-1.3	1.9	0.9	0.5	0.1	-0.2	-0.6	-1.0
Gearing (%)	-17.0%	43.2%	23.6%	13.1%	1.6%	-5.0%	-15.2%	-25.1%

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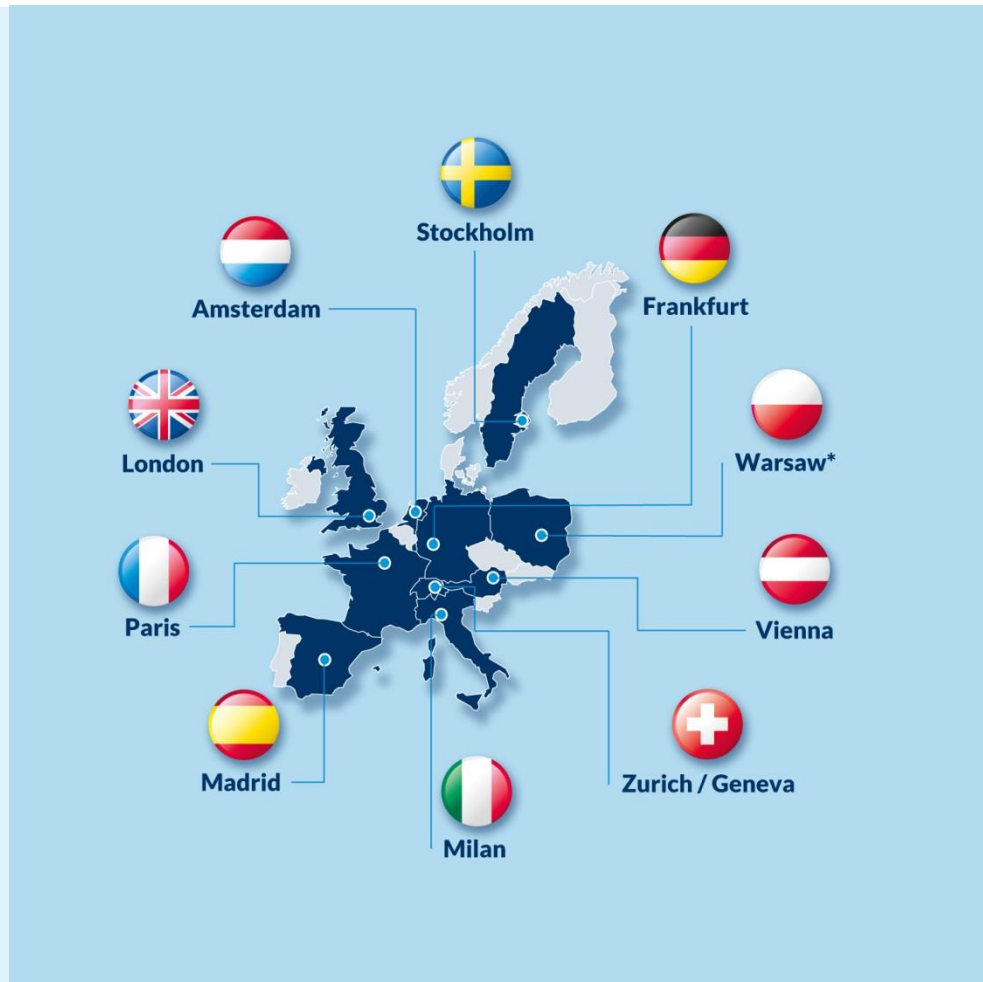
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