

S&T

Germany | IT software & services | MCAP EUR 1.6bn

16 August 2018

Buy

Target Price	EUR 29.00 (25.00)
Current Price	EUR 25.24
Up/downside	14.9%
Change in TP	16.0%
Change in EPS	-6.5% 18E / -

Moving in the right direction

S&T is set for a strong H2, and its mid-term targets also appear to be within reach, as demand remains solid and its strategy is paying off. We confirm our Buy rating and lift our TP to EUR29 (from EUR25).

Solid Q2 – guidance increase likely in Q3

S&T has reported a [solid set of Q2 results](#), as revenues improved by 10% YOY (c. 13% at constant currencies) to EUR219.1m, while EBITDA rose by 31% to EUR19.6m, due to strong performances in IT Services (+22% revenue, 54% EBITDA growth) and IoT Solutions (+7.3% sales, 90.1% EBITDA growth). The EBITDA margin also improved further to 9% (vs. 7.5% in Q2 2017), also helped by forex effects (natural hedging on costs), cost synergies and sales mix effects. As a result, we now expect S&T to beat its guidance of EUR80m EBITDA (KECH: EUR86.4m, 8.6% margin) as growth should remain strong in H2 and forex effects should wane (USD exposure in IoT Solutions is 65%, and 100% in Embedded Systems). The second half of 2018 should increasingly be driven by the IoT Solutions (we expect EUR220m vs. EUR156m sales in H2 vs. H1 2018) and the embedded systems business, which we expect to turn positive in H2 (H1 was -12% sales), also due to some help from M&A (except electronics, Inocybe), recent customer wins, and strong end-markets (i.e. aviation).

Strategy paying off, on track to reach 2023 targets

S&T remains on track to reach its mid-term target to double sales to c. EUR2bn (EUR500m by M&A, remainder organic) by 2023, as demand, especially in the IoT area, remains strong and recent design wins suggest S&T is gaining traction. The strategy to increase the share of higher-margin software (and recurring revenue) in the sales mix (in IoT Solutions and Embedded Systems) should lead to a gradual increase in EBITDA margins to the targeted 10% or higher (vs. 7.7% in 2017). Moreover, M&A remains on the agenda and S&T continues to look for volume suppliers (i.e. recent except electronic acquisition) and technology pearls (recent Inocybe acquisition). However, multiples remain elevated.

Adjusting estimates, catalysts present

We adjust our estimates after Q2 results, include recent M&A (and therefore higher PPA, margin dilution in the short term), roll our model forward, lift our mid- and long-term margin assumptions (+50bps) and increase our DCF-based (8.25% WACC, 2% TG, 11% TM) TP from EUR25 to EUR29. Upcoming catalysts are S&T's CMD on 13 September in London and a strong H2 2018 with a potential guidance increase with Q3 results. Valuation levels remain attractive (28x 2019 EPS, PEG of 1), given the solid growth and margin expansion potential going forward. Buy.

Martin Jungfleisch

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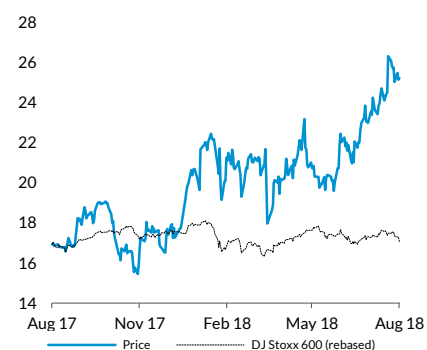
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Market data

Bloomberg: SANT GR	Reuters: SANT1.DE
Market cap (EURm)	1,601
Free float	77%
No. of shares outstanding (m)	63
Avg. daily volume (EURm)	7.1
YTD abs performance	40.3%
52-week high/low (EUR)	26.34/15.45

FY to 31/12 (EUR)	12/18E	12/19E	12/20E
Sales (m)	1,001.7	1,140.7	1,253.9
EBITDA adj (m)	86.4	99.7	116.6
EBIT adj (m)	58.9	71.7	89.6
Net profit adj (m)	44.3	57.1	73.0
Net fin. debt (m)	-87.6	-128.0	-180.9
FCF (m)	32.1	50.0	63.8
EPS adj. and fully dil.	0.69	0.89	1.13
Consensus EPS	0.74	1.01	1.26
Net dividend	0.15	0.17	0.20

FY to 31/12 (EUR)	12/18E	12/19E	12/20E
P/E adj and ful. dil.	36.7	28.4	22.3
EV/EBITDA	17.5	14.8	12.2
EV/EBIT	25.7	20.6	15.8
FCF yield	2.0%	3.1%	4.0%
Dividend yield	0.6%	0.7%	0.8%
Net fin.debt/EBITDA	-1.0	-1.3	-1.6
Gearing	-23.9%	-30.9%	-38.0%
ROIC	9.5%	10.6%	12.8%
EV/IC	3.0	2.8	2.7



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Changes to estimates

We update our estimates on S&T after Q2 results and also include the latest announced M&A in our model. The main effects from M&A will be on the top line in the short term, as we expect the excecet electronics business to add c. EUR60m in 2019E, and Inocybe to add EUR1.7m. However, we expect margins in the IoT Solutions business to be diluted by the recent excecet electronics acquisition, as we do not expect it to generate meaningful EBITDA margins in 2019E (in 2017 it generated an EBITDA loss of EURO.8m in 2017). However, by 2020E we expect Kontron-like synergies to come to fruition and forecast up to a 10% EBITDA margin.

In addition, we have lowered our margin assumption slightly for the IT services and embedded systems segments for 2019E. We have increased our D&A (incl. PPA for acquisitions) assumptions (+EUR2.5m in 2018E to EUR27.5m and +EUR5m in 2019E to EUR28m), which mainly leads to a cut in our EBIT, net income and EPS estimates. We also slightly raised our tax rate assumption from 15% to 16% for 2018/19E.

In terms of free cash flow (FCF), we now expect EUR32m and EUR50m for 2018/19E, respectively, mainly due to higher working capital build-up. Going forward, we expect FCF to equal EBITDA minus capex minus organic growth (NWC).

Risks to our estimates and rating are geopolitical risk (i.e. potential trade wars) due to exposure to cyclical industries and to eastern Europe (mainly IT Service), increased competition in the IoT market as well as slower margin progression as anticipated.

Table 1: Changes to estimates 2018E

	2018 KECH New	2018 KECH Old	% change	Consensus	vs. Consensus
Sales	1,001.7	1,010.1	-0.8%	1,000	0.2%
EBITDA	86.4	86.1	0.4%	85.1	1.6%
% margin	8.6%	8.5%		8.5%	
EBIT	58.9	61.1	-3.5%	61	-3.4%
% margin	5.9%	6.0%		6.1%	
Net income	44.3	47.0	-5.8%	46.4	-4.6%
EPS	0.69	0.74	-6.4%	0.72	-3.8%

Source: Kepler Cheuvreux

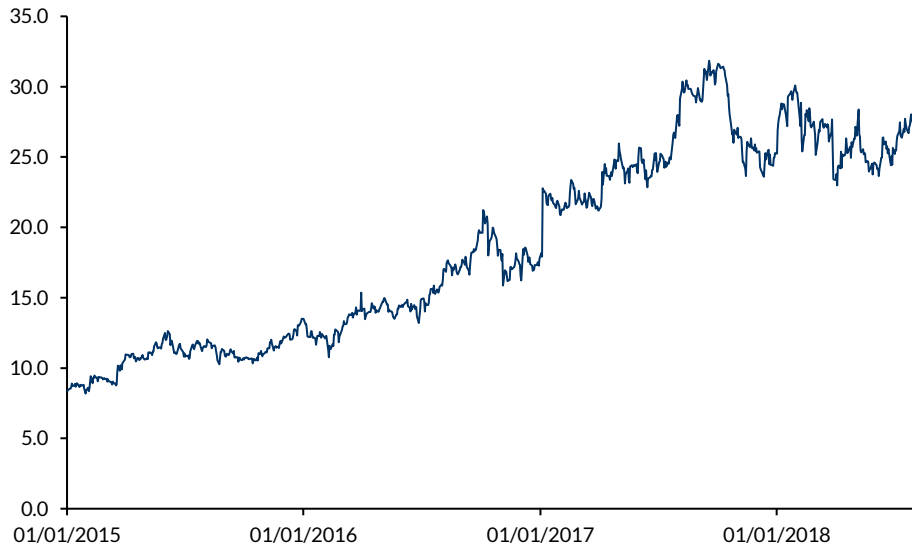
Table 2: Changes to estimates 2019E

	2019 KECH New	2019 KECH Old	% change	Consensus	vs. Consensus
Sales	1,140.7	1,119.1	1.9%	1,099	3.8%
EBITDA	99.7	103.6	-3.8%	102.5	-2.7%
% margin	8.7%	9.3%		9.3%	
EBIT	71.7	80.6	-11.1%	79.2	-9.5%
% margin	6.3%	7.2%		7.2%	
Net income	57.1	64.7	-11.7%	63.5	-10.0%
EPS	0.89	1.01	-11.4%	0.98	-8.7%

Source: Kepler Cheuvreux

Historical valuation levels

Chart 1: S&T historical 1-year forward P/E multiples since 2015



Source: Bloomberg, Kepler Cheuvreux

Key financials

FY to 31/12 (EUR)	12/13	12/14	12/15	12/16	12/17	12/18E	12/19E	12/20E
Income Statement (EURm)								
Sales	338.0	385.5	468.2	503.7	882.0	1,001.7	1,140.7	1,253.9
% Change	-0.4%	14.1%	21.5%	7.6%	75.1%	13.6%	13.9%	9.9%
EBITDA adjusted	20.1	551.5	28.4	34.4	68.1	86.4	99.7	116.6
EBITDA margin (%)	6.0%	143.1%	6.1%	6.8%	7.7%	8.6%	8.7%	9.3%
EBIT adjusted	14.4	16.6	20.6	24.1	41.7	58.9	71.7	89.6
EBIT margin (%)	4.2%	4.3%	4.4%	4.8%	4.7%	5.9%	6.3%	7.1%
Net financial items & associates	-2.2	-0.3	0.5	0.0	0.0	0.0	0.0	0.0
Others	0.0	-1.6	-2.6	-4.0	-6.3	-4.7	-3.2	-2.2
Tax	-0.1	-0.8	-0.8	0.3	-6.0	-8.7	-11.0	-14.0
Net profit from continuing operations	12.0	14.0	17.7	20.4	29.4	45.6	57.5	73.4
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	12.0	14.0	17.7	20.4	29.4	45.6	57.5	73.4
Net profit reported	11.8	12.9	15.8	14.6	22.5	44.3	57.1	73.0
Net profit adjusted	11.8	12.9	15.8	14.6	22.5	44.3	57.1	73.0
Cash Flow Statement (EURm)								
Cash flow from operating activities	9.9	20.6	26.7	61.4	44.9	53.6	73.3	88.6
Capex	-5.8	-5.8	-9.5	-9.3	-23.0	-21.5	-23.3	-24.8
Free cash flow	4.1	14.8	17.2	52.1	21.9	32.1	50.0	63.8
Acquisitions & Divestments	5.2	-4.7	-0.4	-59.2	-11.5	-34.6	0.0	0.0
Dividend paid	-0.3	-4.1	-4.1	-7.8	-7.0	-6.8	-9.6	-10.9
Others	-3.5	2.0	-1.8	37.6	66.5	-5.0	0.0	0.0
Change in net financial debt	5.6	7.9	10.9	22.6	69.9	-14.3	40.4	52.9
Balance Sheet (EURm)								
Intangible assets	44.8	57.1	72.8	183.2	189.9	215.5	207.2	200.7
Tangible assets	9.0	11.4	15.2	27.5	31.9	34.9	38.4	42.8
Financial & other non-current assets	13.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total shareholders' equity	71.2	89.7	102.2	241.1	331.9	365.7	413.6	476.2
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities and provisions	148.9	183.3	216.8	427.7	473.0	506.1	493.0	461.6
Net financial debt	9.3	1.5	-9.4	-32.0	-101.8	-87.6	-128.0	-180.9
Working capital requirement	23.9	90.9	100.7	198.1	211.2	247.2	271.8	290.4
Invested Capital	77.6	159.4	188.6	408.9	433.0	497.6	517.5	533.9
Per share data								
EPS adjusted	0.30	0.32	0.36	0.33	0.43	0.69	0.89	1.14
EPS adj and fully diluted	0.30	0.25	0.30	0.32	0.43	0.69	0.89	1.13
% Change	17.0%	-18.1%	22.4%	7.0%	33.0%	60.3%	29.1%	27.8%
EPS reported	0.30	0.32	0.36	0.33	0.43	0.69	0.89	1.14
Cash flow per share	0.25	0.50	0.61	1.40	0.86	0.84	1.15	1.39
Book value per share	1.76	2.12	2.29	3.50	5.88	5.36	6.11	7.08
Dividend per share	0.06	0.07	0.08	0.10	0.13	0.15	0.17	0.20
Number of shares, YE (m)	39.20	41.00	43.51	48.93	63.44	63.44	63.44	63.44
Ratios								
ROE (%)	18.1%	16.6%	17.0%	11.5%	9.8%	13.7%	15.6%	17.3%
ROIC (%)	14.3%	10.5%	8.9%	6.1%	7.4%	9.5%	10.6%	12.8%
Net fin. debt / EBITDA (x)	0.5	0.0	-0.3	-0.9	-1.5	-1.0	-1.3	-1.6
Gearing (%)	13.1%	1.6%	-9.2%	-13.3%	-30.7%	-23.9%	-30.9%	-38.0%
Valuation								
P/E adjusted	7.9	9.0	12.2	22.8	32.0	36.4	28.2	22.1
P/E adjusted and fully diluted	7.9	11.6	14.8	23.4	32.4	36.7	28.4	22.3
P/BV	1.4	1.3	1.9	2.2	2.4	4.7	4.1	3.6
P/CF	9.5	5.7	7.3	5.4	16.1	30.1	22.0	18.2
Dividend yield (%)	2.5%	2.5%	1.8%	1.3%	0.9%	0.6%	0.7%	0.8%
FCF yield (%)	4.4%	12.7%	8.9%	14.1%	2.5%	2.0%	3.1%	4.0%
EV/Sales	0.3	0.3	0.4	0.7	0.9	1.5	1.3	1.1
EV/EBITDA	5.1	0.2	6.5	9.8	11.4	17.5	14.8	12.2
EV/EBIT	7.2	7.2	8.9	14.0	18.7	25.7	20.6	15.8

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Prices in this report are taken as of the previous day's close (to the date of this report) on the home market unless otherwise stated.

Companies mentioned

Stock	ISIN	Currency	Price
S&T	AT0000A0E9W5	EUR	25.24

Source: Factset closing prices of 15/08/2018

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Name of the Research Analyst(s): Martin Jungfleisch

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Rating Breakdown	A	B
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Hold	37%	39%
Reduce	13%	12%
Not Rated/Under Review/Accept Offer	3%	9%
Total	100%	100%

Source: KEPLER CHEUVREUX

A: % of all research recommendations

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	29/03/2018 08:52	Equity Research	Under Review	19.50	20.06
	04/04/2018 08:24	Equity Research	Buy	21.50	18.66
	07/05/2018 08:15	Equity Research	Buy	25.00	21.64

Credit research does not issue target prices. Left intentionally blank.

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Reduce: There is an expected downside.

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