TXT e-solutions

FY14 results

Expanding into Asia Pacific

Software & comp services

TXT's FY14 results reflect the impact of the tough economic environment on TXT Perform earlier in the year. Efforts to strengthen the team in North America are starting to pay off and the recently announced investment in Asia Pacific should support growth in the medium term. We expect increased investment in international expansion and product development to weigh on profitability in FY15, but this should position the company for stronger international growth in the medium to long term.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/13	52.6	4.8	0.45	0.25	21.4	2.6
12/14	54.4	4.0	0.29	0.25	32.9	2.6
12/15e	58.3	5.1	0.37	0.26	25.9	2.7
12/16e	60.7	6.3	0.49	0.27	19.9	2.8

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

FY14: Lower licensing depresses margins

FY14 was a year of mixed fortunes: the tough environment for fashion and retail hit demand in Q2, but order intake improved through the course of H214. TXT reported FY14 revenue slightly higher than our forecast, with upside from TXT Next, which grew Q4 revenues 14% y-o-y. Higher investment in R&D in Q414 took EBIT below our forecast which, combined with a higher than expected tax rate (20% vs our 15%), resulted in normalised EPS 12% below our forecast. Our normalised forecasts excluded the one-off income from the €1.5m purchase price retention.

FY15: Investing in product & geographic expansion

During FY14 TXT reorganised and strengthened its North American operations; initial signs are encouraging, with a growing pipeline. In Q115 the company announced plans to open an office in Hong Kong to service the Asia Pacific region. The initial focus will be on servicing existing customers with Asia Pacific operations, with the ultimate aim of signing up local companies; we would therefore not expect a revenue contribution before the end of FY15. TXT expects to increase R&D investment in FY15 – areas of focus include in-memory processing, expansion of the AgileFit methodology and development of additional functionality for CPG and manufacturing companies.

Valuation: Licensing growth key to upside

The stock trades on a P/E of 25.9x FY15e and 19.9x FY16e normalised EPS. This is at a small discount to global supply chain software vendors and at a premium to European IT services companies, which is reasonable considering the split of the business. TXT has a strong cash position and we forecast a dividend yield of at least 2.5% for FY15 and FY16. We view FY15 as an investment year as TXT puts in place the building blocks to support growth in the medium term. Key milestones to assess progress will include a growing order backlog in North America, hiring key staff in the Hong Kong office, and signing the first local customer in Asia Pacific. The company continues to assess acquisitions in the TXT Next business.

9 March 2015

Price	**€9.69**
Market cap	**€101m**

Net cash (€m) at end FY14	8.5
Shares in issue	10.4m
Free float	65%
Code	TXT
Primary exchange	Borsa Italiana (STAR)
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	10.6	20.5	(15.2)
Rel (local)	2.1	6.8	(21.3)
52-week high/low		€11.4	€6.9

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 events

AGM	22 April 2015

Analysts

Katherine Thompson +44 (0)20 3077 5730

Dan Ridsdale +44 (0)20 3077 5729

tech@edisongroup.com

Edison profile page

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Review of FY14 results

TXT reported 3.5% revenue growth for FY14, with 3.1% growth in TXT Perform and 4.2% in TXT Next. We exclude the €1.5m retention of part of the Maple Lake purchase price, which arose when two of the original sellers left before the agreed lock-in period, instead treating this as exceptional income. Licence & maintenance revenues declined 1.9% over the year, whereas service revenues grew 5.2% y-o-y. The lower proportion of licence & maintenance revenues resulted in a lower gross margin compared to FY13. Operating expenses before depreciation and amortisation totalled €22.6m, up 5.5% y-o-y, with the main increase from higher investment in sales and marketing. The tax rate of 20% was higher than our 15% forecast and a contrast to the 3% tax credit in the previous year. Net cash was effectively flat year-on-year, after paying out €2.6m in dividends and funding higher working capital. The company announced a full year dividend of €0.25, flat versus FY13. After the dividend is paid on 18 May, TXT will issue one free share for every 10 owned.

Exhibit 1: FY14 results highlights

€m	FY14e	FY14a	FY13a	y-o-y
Revenues	54.0	54.4	52.6	3.5%
TXT Perform	32.8	32.6	31.7	3.1%
TXT Next	21.2	21.8	20.9	4.2%
Gross margin	51.6%	51.3%	52.7%	
EBIT	4.5	4.3	5.2	-18.9%
EBIT margin	8.4%	7.8%	10.0%	
Normalised net income	3.6	3.2	4.9	-35.0%
Normalised EPS - FD (€)	0.33	0.29	0.45	-34.9%
Net income	4.7	4.2	4.6	-10.1%
Basic EPS (€)	0.45	0.40	0.44	-9.9%
Net cash	9.8	8.5	8.6	-1.3%

Source: TXT e-solutions, Edison Investment Research

Business update

TXT Perform

TXT Perform achieved 3.1% revenue growth in FY14. Q414 revenues grew 6.6% y-o-y, driven by strong licensing towards the end of the year (Q4 licence & maintenance revenues +23.5% y-o-y). The division saw a slowdown in licensing in Q2, with demand recovering through the course of H214.

Asia Pacific expansion

The company announced that it is planning to open an office in Hong Kong in H115 from where it will service existing international clients with operations in Asia Pacific and will also market to local companies. The company had not previously targeted local companies, as the view was that these companies were focused on growing the number of branches across China and were not in a position to pay for planning software. Management has observed that many of these companies are maturing, and shifting their focus from revenue growth to profit growth, with the goal of improving profitability to levels similar to Western competitors. Management sees more willingness from these local companies to adopt end-to-end planning tools and is now aiming to build up its sales and delivery capability in the region, with a mix of corporate and local staff. TXT Perform software already has the capability to deal with Chinese characters, although the companies that TXT will initially target are likely to operate in English. There may be some scope for localisation of the software, but there is no plan to do so in the near term.

North America – efforts to strengthen team bearing fruit

To accelerate North American sales, in 2014 TXT hired several new sales and marketing employees. This included the January hiring of Peter Charness as senior vice president of North America, who has also taken 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).

The company is seeing the launch of larger new projects from existing customers and the pipeline has improved over the year. In January 2015, the company exhibited at the National Retail Federation (NRF) conference in New York, generating a promising number of qualified leads.

R&D: Good acceptance of AgileFit; in-memory technology going live

The company introduced its AgileFit methodology last year, which has been well received in Europe and North America. For large customers, AgileFit provides a good way to fill gaps in software functionality. For mid-sized customers, the technology provides a quick way to implement planning software. The company used AgileFit for implementation with three customers in 2014: Miroglio, Bata and Pandora. In 2015, the company plans to develop AgileFit methodology for a wider range of processes.

The company has been developing in-memory processing, which should improve the responsiveness of the software for more interactive processes. Software using this technology will be going live at a customer in the coming weeks.

Bolstering sales & operation planning for CPG and manufacturers

As well as providing planning software to the retail sector, TXT Perform develops and supplies sales & operating planning (S&OP) software to CPG and consumer-facing industrial companies. The company has decided to give this part of the business more autonomy, including the ability to develop software specialisms for the verticals served.

TXT Next

TXT Next grew revenues 4.2% y-o-y in FY14 and 14.1% in Q414. The business saw a good performance across Aerospace & High Tech Manufacturing and Banking & Finance. The division continues to consider acquisitions in Europe to diversify the customer base and add local presence.

Outlook and changes to estimates

The company has seen a more uncertain international economic environment since the summer of 2014, but by strengthening its position in North America and building on its current customer base it believes it can outgrow the market. By shifting the focus of the S&OP business, the company is hoping to benefit from the improving situation for manufacturing companies. In terms of order book, TXT Perform has good visibility over services, but has less visibility over the timing of licence orders.

We make the following changes to forecasts:

- Revenues: we have reduced our TXT Perform revenue forecast for FY15 to reflect the current backlog. We assume continued steady growth in TXT Next. For FY16, we forecast modest growth of 4% in both divisions – it is possible that recent investment in North America and ongoing investment in Hong Kong could drive a faster rate of licensing in TXT Perform.
- Operating costs: the company has decided to increase R&D investment – we increase our FY15 forecast from €4.4m to €5.1m and maintain FY16 at the same rate. The company is

moving all of its subsidiaries onto an SAP ERP system through the course of FY15 – this will cost c €0.5m in licence and implementation costs. Consequently our G&A forecast for FY15 increases from €7.2m to €7.6m before falling back to €7.3m in FY16.

- Tax rate: we leave our forecast 20% for FY15 and use the same rate for FY16.
- EPS: the higher rate of investment in FY15, combined with slightly lower revenues, drives an 18% cut to normalised EPS (27% growth y-o-y). In FY16 we forecast EPS growth of 30%.
- Dividend: we forecast a small increase in the dividend of 1c in both FY15 and FY16.

Exhibit 2: Changes to estimates

	FY15e old	FY15e new	change	y-o-y	FY16e new	y-o-y
Revenues (€m)	58.8	58.3	-0.9%	7.2%	60.7	4.2%
TXT Perform	36.5	35.9	-1.6%	10.0%	37.5	4.3%
TXT Next	22.3	22.4	0.4%	2.9%	23.3	3.9%
Gross margin	51.7%	51.7%			51.7%	
Gross profit	30.4	30.2	-0.7%	8.0%	31.4	4.1%
EBITDA (€m)	7.1	6.0	-15.6%	13.0%	7.0	17.7%
EBITDA margin	12.0%	10.3%			11.6%	
Normalised EBIT (€m)	6.3	5.2	-18.1%	21.5%	6.4	24.5%
Normalised EBIT margin	10.7%	8.9%			10.6%	
Normalised net income (€m)	5.0	4.1	-18.4%	26.7%	5.1	25.0%
Normalised EPS (€)	0.46	0.37	-18.3%	27.1%	0.49	30.3%
Net cash (€m)	11.9	10.5	-11.9%	23.6%	12.6	20.8%
Dividend (€)	0.27	0.26	-3.7%	4.0%	0.27	3.8%

Source: Edison Investment Research

Exhibit 3: Financial summary

	€'000s	2010	2011	2012	2013	2014	2015e	2016e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		37,458	40,138	46,499	52,560	54,378	58,300	60,720
Cost of sales		(18,757)	(19,522)	(22,351)	(24,854)	(26,455)	(28,143)	(29,327)
Gross profit		18,701	20,616	24,148	27,706	27,923	30,158	31,393
EBITDA		2,769	4,397	5,322	6,263	5,292	5,978	7,033
Operating Profit (before amort and except)		(776)	843	4,283	5,241	4,252	5,168	6,433
Amortisation of acquired intangibles		0	0	0	(285)	(285)	(285)	(285)
Exceptionals and other income		13	(4,581)	939	0	1,500	0	0
Other income		0	0	0	0	0	0	0
Operating Profit		(763)	(3,738)	5,222	4,956	5,467	4,883	6,148
Net Interest		(198)	72	(37)	(435)	(249)	(100)	(100)
Profit Before Tax (norm)		(974)	915	4,246	4,806	4,003	5,068	6,333
Profit Before Tax (FRS 3)		(961)	(3,666)	5,185	4,521	5,218	4,783	6,048
Tax		255	(591)	(188)	121	(1,046)	(957)	(1,210)
Profit After Tax (norm)		(719)	324	4,092	4,927	3,201	4,054	5,067
Profit After Tax (FRS 3)		(706)	(4,257)	4,997	4,642	4,172	3,826	4,839
Average Number of Shares Outstanding (m)		10.3	10.1	10.0	10.5	10.4	10.4	10.4
EPS - normalised (c)		(7)	3	41	47	31	39	49
EPS - normalised fully diluted (c)		(6)	3	37	45	29	37	49
EPS - (IFRS) (c)		2	140	50	44	40	37	47
Dividend per share (c)		0.0	100.0	20.0	25.0	25.0	26.0	27.0
Gross margin (%)		49.9%	51.4%	51.9%	52.7%	51.3%	51.7%	51.7%
EBITDA Margin (%)		7.4	11.0	11.4	11.9	9.7	10.3	11.6
Operating Margin (before GW and except) (%)		-2.1	2.1	9.2	10.0	7.8	8.9	10.6
BALANCE SHEET								
Fixed Assets		14,328	7,735	18,570	17,850	18,019	17,544	17,279
Intangible Assets		11,526	6,561	16,621	15,370	15,078	14,583	14,318
Tangible Assets		1,528	819	1,154	1,118	1,249	1,269	1,269
Other		1,274	355	795	1,362	1,692	1,692	1,692
Current Assets		28,876	32,145	36,769	34,914	34,892	37,186	39,761
Stocks		793	661	1,388	1,451	1,820	1,820	1,820
Debtors		21,453	15,083	19,562	18,642	20,768	21,563	22,458
Cash		6,630	14,181	15,819	14,821	12,304	13,803	15,483
Other		0	2,220	0	0	0	0	0
Current Liabilities		(17,719)	(14,049)	(20,651)	(17,864)	(17,451)	(18,544)	(19,218)
Creditors		(15,615)	(12,292)	(15,155)	(14,512)	(15,297)	(16,390)	(17,064)
Short term borrowings		(2,104)	(1,757)	(5,496)	(3,352)	(2,154)	(2,154)	(2,154)
Long Term Liabilities		(8,398)	(5,567)	(8,666)	(6,965)	(6,491)	(5,991)	(5,491)
Long term borrowings		(3,870)	(2,155)	(4,301)	(2,896)	(1,685)	(1,185)	(685)
Other long term liabilities		(4,528)	(3,412)	(4,365)	(4,069)	(4,806)	(4,806)	(4,806)
Net Assets		17,087	20,264	26,022	27,935	28,969	30,196	32,331
CASH FLOW								
Operating Cash Flow		9,967	19,265	2,760	7,630	5,404	6,275	6,812
Net Interest		(198)	166	(37)	(435)	(249)	(100)	(100)
Tax		255	390	64	(1,615)	(1,344)	(957)	(1,210)
Capex		(2,340)	(2,159)	(405)	(483)	(615)	(620)	(620)
Acquisitions/disposals		(137)	2,403	(8,450)	19	0	0	0
Financing		324	(106)	1,690	(755)	(597)	0	0
Dividends		0	(10,292)	0	(2,107)	(2,615)	(2,599)	(2,703)
Net Cash Flow		7,871	9,667	(4,378)	2,254	(16)	1,999	2,180
Opening net debt/(cash)		7,248	(723)	(10,266)	(6,023)	(8,575)	(8,465)	(10,464)
HP finance leases initiated		0	0	0	0	0	0	0
Other		100	(124)	135	298	(94)	0	0
Closing net debt/(cash)		(723)	(10,266)	(6,023)	(8,575)	(8,465)	(10,464)	(12,644)

Source: TXT e-solutions, Edison Investment Research

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