

Keywords Studios

12% organic revenue growth despite COVID-19

FY20 trading update

Software & comp services

28 January 2021

Price **2,704p**

Market cap **£2.01bn**

€1.13/£

Approx. net cash (€m) at 31 December 2020 (excluding lease liabilities) 100.0

Shares in issue 74.4m

Free float 90%

Code KWS

Primary exchange AIM

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (5.9) 22.5 94.8

Rel (local) (6.5) 6.6 115.9

52-week high/low 2,942p 1,232p

Business description

Keywords Studios is the largest and most diverse supplier of outsourced technical and creative services to the games industry. Through regular acquisitions, the company is building its scale, geographic footprint and delivery capability to become the 'go-to' supplier across the industry.

Next event

FY20 results 24 March 2021

AGM May 2021

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Management has confirmed that FY20 revenues and adjusted PBT will be marginally ahead of guidance, with revenues of €373m (guidance c €367m) and adjusted PBT of €55m (guidance c €52m). This outperformance has been driven by a strong close to the year, together with an additional revenue contribution from December's M&A. Given the headwinds from COVID-19 in FY20, underlying organic revenue growth of 12% (H120: 8.0%, FY19: 15.5%) is a hugely resilient performance. The group is set well for FY21 and, with a growing next-gen console base in FY22/23, the medium-term outlook appears bright. With net cash of c €100m, Keywords remains well placed to execute further M&A deals in FY21.

Year end	Revenue (€m)	PBT* (€m)	EPS* (c)	DPS (p)	P/E (x)	Yield (%)
12/18	250.8	37.9	45.5	1.61	67.1	0.06
12/19	326.5	40.9	48.8	0.58	62.6	0.02
12/20e	373.0	55.0	61.2	0.00	50.0	N/A
12/21e	464.5	67.8	71.5	1.91	42.7	0.07

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

Margin recovery in H220 set to persist in H121

FY20 revenues of €373m and adjusted PBT of €55m indicate a significant recovery in FY20 adjusted PBT margin to 14.7% (H120: 12.5%, FY19: 12.5%), implying an H220 margin of 16.7%. This bodes well for margins in FY21, with a similar environment expected in H121 to H220, although costs are likely to start to normalise again in H221. Management attributed the underlying margin improvement to operational leverage, effective cost control and a reduction in the normal cost base due to COVID-19 (eg travel, marketing).

Management noted a strong finish to the year, despite continuing delivery challenges in audio and localisation. Keywords remains well capitalised with net cash at 31 December 2020 of c€100m (H120: €101m, FY19: net debt of €17.9m), together with €100m of undrawn facilities, having spent cash of €38m (net of cash acquired) on its seven acquisitions in FY20 (of which, six were in H220).

Model updated, estimates unchanged

We have updated our FY20 estimates to bring them into line with management guidance and also reflected contributions from the last acquisitions of the year (High Voltage Software, Indigo Pearl and Jinglebell) in December. However, apart from the consequential increase in the starting revenue run-rate, we have otherwise left our assumptions for FY21 and FY22 unchanged at this stage.

Valuation: Earnings to rise with continuing M&A

Keywords' shares trade on an FY21e P/E of 42.7x, falling to 37.6x in FY22e, in line with its UK and European games industry peers. Although this is a demanding valuation, we expect the recent next-gen console launches to lead to a period of heightened game releases, benefiting underlying growth in the period from FY21–23. Supplemented by its proven buy-and-build strategy, we expect earnings to rise, lowering valuation multiples as deals are completed in FY21 and beyond.

Exhibit 1: Financial summary

	€'000s	2018	2019	2020e	2021e	2022e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		250,805	326,463	373,018	464,520	520,263
Cost of Sales		(154,997)	(206,234)	(230,576)	(288,307)	(322,322)
Gross Profit (inc multimedia tax credits)		95,808	120,229	142,442	176,214	197,941
EBITDA (adjusted)		43,729	57,611	72,902	89,703	100,821
EBITDA (reported)		34,304	43,375	63,190	77,875	87,811
Operating Profit (before amort. and except.)		38,916	42,983	58,513	70,303	79,321
Amortisation of acquired intangibles		(6,872)	(7,318)	(11,324)	(14,269)	(15,981)
Exceptionals		(5,296)	(4,348)	(2,370)	0	0
Other (incl share based payments)		(4,129)	(9,775)	(10,753)	(11,828)	(13,011)
Operating Profit		22,619	21,542	34,066	44,207	50,330
Net Interest		(1,316)	(2,513)	(3,500)	(2,500)	(2,500)
Forex		791	(1,658)	0	0	0
Profit Before Tax (norm)		37,911	40,913	55,013	67,803	76,821
Profit Before Tax (FRS 3)		22,094	17,371	30,566	41,707	47,830
Tax		(7,191)	(7,462)	(10,034)	(12,366)	(14,011)
Profit After Tax (norm)		30,720	33,451	44,979	55,437	62,810
Profit After Tax (FRS 3)		14,903	9,909	20,533	29,340	33,819
Average Number of Shares Outstanding (m)		64.3	65.1	69.8	74.6	74.9
EPS - normalised (c)		45.5	48.8	61.2	71.5	81.3
EPS - normalised fully diluted (c)		43.7	47.2	58.8	69.3	79.0
EPS - (IFRS) (c)		23.2	15.2	29.4	39.3	45.1
Dividend per share (p)		1.61	0.58	0.00	1.91	2.11
Gross Margin (%)		38.2%	36.8%	38.2%	37.9%	38.0%
EBITDA Margin (%)		13.7%	13.3%	16.9%	16.8%	16.9%
Operating Margin (before GW and except.) (%)		15.5%	13.2%	15.7%	15.1%	15.2%
PBT Margin (%)		15.1%	12.5%	14.7%	14.6%	14.8%
BALANCE SHEET						
Fixed Assets		198,215	223,992	250,322	260,730	262,758
Intangible Assets		180,086	196,769	221,445	223,049	214,529
Tangible Assets		15,002	22,163	23,817	32,621	43,169
Investments		3,127	5,060	5,060	5,060	5,060
Current Assets		100,348	120,483	238,536	276,058	332,056
Stocks		0	0	0	0	0
Debtors		37,019	43,243	47,433	53,125	59,500
Cash		39,870	41,827	152,258	179,427	223,830
Other		23,459	35,413	38,845	43,506	48,727
Current Liabilities		(95,031)	(49,551)	(49,948)	(33,311)	(26,102)
Creditors		(54,960)	(49,471)	(49,868)	(33,231)	(26,022)
Short term borrowings		(40,071)	(80)	(80)	(80)	(80)
Long Term Liabilities		(11,158)	(71,528)	(71,194)	(73,194)	(75,194)
Long term borrowings		(230)	(59,671)	(59,671)	(59,671)	(59,671)
Other long-term liabilities		(10,928)	(11,857)	(11,523)	(13,523)	(15,523)
Net Assets		192,374	223,396	367,716	430,283	493,518
CASH FLOW						
Operating Cash Flow		33,954	46,069	67,993	80,734	89,510
Net Interest		(502)	(9,411)	(6,263)	(3,425)	(2,276)
Tax		(6,304)	(13,288)	(10,034)	(12,366)	(14,011)
Capex		(9,440)	(13,145)	(11,265)	(18,704)	(20,948)
Acquisitions/disposals		(25,766)	(27,762)	(40,000)	(17,637)	(8,289)
Financing		0	0	110,000	0	0
Dividends		(1,080)	(1,197)	0	(1,432)	(1,582)
Net Cash Flow		(10,090)	(18,734)	110,432	27,169	43,403
Opening net debt/(cash)		(11,094)	431	17,924	(92,508)	(119,677)
Forex gain on cash		(3)	1,293	0	0	0
Other		(1,432)	(52)	0	0	0
Closing net debt/(cash)		431	17,924	(92,508)	(119,677)	(163,079)

Source: Company accounts, Edison Investment Research

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