

## Vectron Systems

IT hardware

23 May 2017

### Cashing in on online opportunity

Vectron's core point of sale (POS) business generated strong growth in revenues and earnings in FY16, and should continue to benefit from several growth drivers in the short to medium term. With adoption by 2-3% of its customer base, Vectron's existing online marketing solution, bonVito, is close to breaking even. The recently announced partnership with Coca-Cola to support its GetHappy loyalty app has the potential to add high-margin recurring revenues from the end of FY17.

### Hospitality-focused POS supplier

Focused on the hospitality market in German-speaking Europe, Vectron's core POS business has shown strong growth in revenues and profitability over the last two years, helped by a combination of internal product development and changes in regulation relating to electronic cash registers. Vectron recently bought 75% of Posmatic, an mPOS provider that supplies its software on a subscription basis. The company's online marketing platform, bonVito, provides participating merchants with loyalty and marketing services integrated with their Vectron tills. With 2,671 participating merchants and 5m cards in circulation, the company expects this service to break even soon.

### Growth from core business and new initiatives

In the core business, Vectron is benefiting from regulation against electronic cash register-related tax evasion that is driving software and hardware upgrades – this is likely to be a multi-year process. Growing demand for the Duratec system is driving incremental sales and should help Vectron's international expansion plans. The partnership with Coca-Cola will see the bonVito platform being used to upgrade Coca-Cola's GetHappy loyalty app, turning it into a comprehensive provider of online marketing services to the hospitality industry. Successful adoption of the new app (launch targeted for the end of FY17) should generate a high-margin recurring revenue stream for Vectron and could accelerate sales of its POS systems.

### Valuation: Factoring in online marketing success

On consensus forecasts (which mask a wide range of forecasts), Vectron is trading at a premium to traditional POS suppliers and more in line with online service providers to the hospitality market. Evidence of successful adoption of the new GetHappy app, which should start to contribute to earnings in FY18, will be key to upside to the stock.

#### Consensus estimates

Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/15	25.9	1.8	0.79	0.45	162.0	0.4
12/16	33.7	3.0	1.19	N/A	107.6	N/A
12/17e	42.5	8.6	3.48	0.37	36.8	0.3
12/18e	52.2	12.2	5.21	0.40	24.6	0.3

Source: Bloomberg, company accounts

Price €128  
Market cap €211m

#### Share price graph



#### Share details

Code V3S  
Listing Deutsche Börse Scale  
Shares in issue 1.65m  
Last reported net cash as at 31 December 2016 €7.2m

#### Business description

Vectron Systems produces high-end, proprietary POS systems for the hospitality sector. Vectron is also diversifying into providing systems, designed for online marketing services, which has been given impetus recently through a partnership with Coca-Cola.

#### Bull

- Flexible, comprehensive POS systems.
- Regulatory tailwinds.
- Partnership with Coca-Cola.

#### Bear

- Dependent on the German economy.
- Management owns more than 50% of Vectron.
- bonVito is loss-making.

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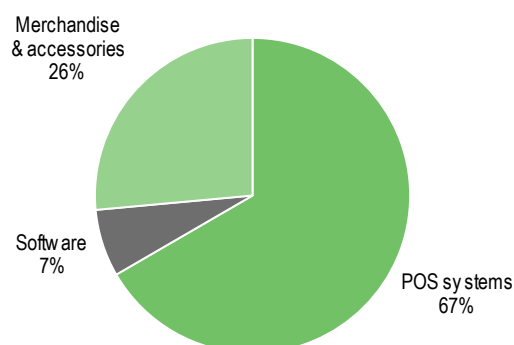
## Company description: High-end POS systems

Vectron Systems is a German technology company that provides both hardware and software for POS systems, with a focus on the hospitality sector. The company has sales representation in 30 countries, with over 190,000 installations in more than 30 countries to date, making it one of the largest POS operators in Europe. The company also offers an online marketing service, bonVito, and has partnered with Coca-Cola to support its GetHappy app.

Vectron Systems was founded in 1990 by current management (Mr Jens Reckendorf and Mr Thomas Stümmeler) and listed in 2007. In March 2017, the company moved from the Entry Standard to the new Scale segment of the Deutsche Börse. The company's headquarters are in Münster, Germany, where it also manufactures its products. It currently has 167 employees.

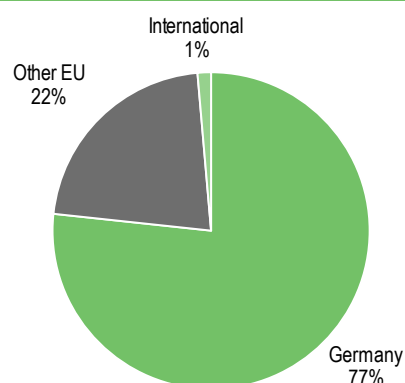
## Focus on German-speaking Europe

**Exhibit 1: Revenues by segment, FY16**



Source: Vectron Systems accounts

**Exhibit 2: Revenues by geography, FY16**



Source: Vectron Systems accounts

Vectron derives two-thirds of its revenues from the sale of POS systems. This figure also includes the pre-installed proprietary software necessary for the terminals to function. The software segment accounted for 7% of revenues in FY16, and includes software upgrades for the POS systems in addition to back office functions such as the 'Commander communications software', which interconnects all Vectron POS systems across branches, and amalgamates the data. The final reported segment is that of merchandise and accessories, which is made up of a combination of Vectron products such as customer display screens and contactless card readers, in addition to the resale of third-party products such as printers, scanners and cash drawers, all of which can be networked with the Vectron POS systems.

The company generates the vast majority of its revenues in Europe. While Germany and Austria are the two principal markets, it also has a growing presence in Benelux, France, Spain and the UK. The company is keen to grow the business outside of Germany, and we note non-German sales rose 9% in FY16.

Vectron designs the POS systems, outsources the manufacturing of all necessary hardware components, and undertakes final assembly of the systems at its facility in Münster. It typically manufactures c 16,000 systems per annum.

## Market leader for the hospitality sector

Vectron is the market leader in the production of sophisticated POS systems for the hospitality sector, including bars, restaurants, cafes and bakeries. Aside from performing key functions such as processing sales and cashing, Vectron products provide a suite of additional functionality. The POS

systems are highly customisable, and provide management with tools such as resource planning and employee attendance records. The products are also easy to network together, including interfaces with peripheral equipment such as cash drawers, card readers, printers and drink-dispensing systems, and, importantly, with terminals in other branches. Furthermore, all the systems work without an internet connection, with all data saved within the devices. This greatly enhances the security of the Vectron product suite, as it is significantly harder to intercept signals (and customer information) without any connection to the internet. Perhaps most importantly, the Vectron product offering is highly reliable, both in terms of the durability of the products (they are water- and dust-proof, and shock-resistant) and in terms of how few faults occur within the systems. This is of critical importance to the hospitality sector, as many of Vectron's target audience will only have a single cash register per establishment. Clients' demands range from single installations to networks of over 1,000 cash registers.

#### Exhibit 3: Examples of brands that use Vectron POS systems



Source: Vectron Systems

## Indirect sales network brings scale

The company sells its products through a network of approximately 300 local resellers, with presence in more than 30 countries. The largest of these resellers was responsible for approximately 5% of sales in 2016. Any deals originated by Vectron's direct sales team are fulfilled via a reseller. Resellers provide upfront and ongoing support to end customers. Vectron generates revenues from the upfront sale of POS systems, peripherals and software, as well as any follow-on software upgrades. As many of the end customers using Vectron's systems are small (sometimes just a single till in one shop), using resellers is a more cost-effective way to access the market and support customers over the longer term.

## Growth strategy

The company is focused on growing the core business as well as driving new initiatives in online marketing. We see several drivers of growth in the core business:

- a new product, Duratec, to address the lower end of the market;
- the introduction of mPOS solutions; and
- regulatory changes driving software and/or hardware upgrades.

The launch of bonVito was the company's first entry into online marketing. The recent announcement of a partnership with Coca-Cola adds the potential to grow revenues and EBITDA on a more significant basis. Vectron will be using its bonVito technology platform to upgrade the functionality of Coca-Cola's GetHappy loyalty app in order to create a comprehensive online marketing tool for merchants.

Both initiatives have the potential to add recurring revenues to a business that traditionally has a very low level of recurring revenue.

## Expanding into the lower end of the market

Due to the high-end nature of its core POS product, Vectron has historically targeted the upper end of the market. This has required that resellers are well trained and experienced in implementing the systems for customers. The company realised that not all end customers need the full level of functionality offered by the Vectron POS systems, and that expansion outside of DACH would require the company to train and support an ever-growing number of resellers in multiple countries and languages. It therefore decided to develop a simplified version of the Vectron system, branded Duratec and targeted at the mid-market – this was launched in 2013.

The Duratec system provides similar functionality to the Vectron-branded products (albeit without the same level of customisability) at lower price points. Critically, Duratec products use the same underlying software as the Vectron-branded products, enabling a customer to network terminals of both brands together, even across different branches. Sales of Duratec products increased 57% y-o-y to €1.0m in FY16, and a further 235% y-o-y to €0.57m in Q117. This figure is entirely derived from German sales, as Vectron has yet to launch Duratec products abroad, a milestone it expects to achieve in H217. Furthermore, the vast majority of these sales were made via new resellers who did not already market the Vectron brand. As a result, we see these sales as being largely incremental, rather than cannibalising Vectron-branded revenues, as the two brands are often sold via different sales channels, and target different end customers, which require differing levels of sophistication in their POS networks.

## Increasing shift to mPOS triggers Posmatic acquisition

The POS terminal industry is seeing growing numbers of retailers turning to mPOS (mobile POS) systems, which use software for standard consumer hardware such as smartphones, tablets and PCs. While not as sophisticated as dedicated POS hardware, it costs the retailer less to implement and maintain, and has been experiencing rapid growth in recent years. GM Insights [forecasts](#) that the mPOS market will grow at a 19% CAGR from 2016-23 as this type of solution gains market share.

Vectron's approach until recently was to offer its own handheld devices as well as a mobile app. Surprisingly the mobile app did not reduce demand for handheld devices and in fact led to increased demand for traditional cash tills. However, some customers want a full Apple-based solution (hardware and app combined), which prompted Vectron to acquire 75% of German software company Posmatic GmbH in November 2016 for a six-figure sum. Posmatic designs and sells POS software for Apple hardware such as iPhones and iPads and sells this for a monthly fee. This should add a level of recurring revenue.

## Regulatory tailwinds drive organic growth

Regulation is being introduced in many countries to reduce the incidence of tax fraud arising from the under-reporting of sales made via electronic cash registers. In Germany, as of 2017, new GoBD<sup>1</sup>/GDPdU<sup>2</sup> legislation imposed rules on the production and storage of financial materials such as electronic receipts, and also ensures verifiability of all the documents that are made. There is further draft legislation scheduled for 2020 that will permit unannounced reviews of POS systems to ensure they are compliant. The Austrian government approved similar measures as of 2016; it requires all taxable businesses to issue customers with a receipt and maintain a data collection log (DCL) of all transactions. Furthermore, since April 2017, all POS systems must be protected against manipulation by a tamperproof security device.

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<sup>1</sup> GoBD: Grundsätze zur ordnungsmässigen Führung und Aufbewahrung von Büchern, Aufzeichnungen und Unterlagen in elektronischer Form sowie zum Datenzugriff

<sup>2</sup> GDPdU: Grundsätze zum Datenzugriff und zur Prüfbarkeit digitaler Unterlagen

All new Vectron POS products are fully compliant with both sets of regulations. Many older Vectron systems can be made compliant via a software upgrade. Those customers using very old Vectron machines may need to upgrade to new machines (we note that Vectron systems have a typical life of seven to 10 years). This tailwind is likely to be felt right up to 2020, as businesses upgrade their existing POS infrastructure to remain compliant. However, it is very difficult to predict the timing of the revenue opportunity, as many customers may wait as long as possible to upgrade their current POS systems before they are deemed non-compliant by the German or Austrian authorities.

## **Integrated internet marketing and loyalty schemes**

Vectron's proprietary internet marketing offering, bonVito, is a white-label service that enables customers to create their own local loyalty schemes. It provides tools for improved customer retention, customer account cards, e-payments and online reservations and orders.

The Vectron POS systems are continuously connected to the bonVito platform, enabling tailored marketing campaigns to be installed automatically across a client's network of POS systems. These campaigns can then be fully automated by the POS systems themselves, without requiring additional work from employees.

In signing up to bonVito, consumers benefit from personalised reward schemes, thereby improving customer loyalty. In turn, the operator of the POS system (Vectron's clients) can accrue valuable data on their customers and their buying behaviour. The same POS terminal can then be used to perform analytics of this data to measure the efficacy of different campaigns. Vectron charges a transaction fee on all purchases made via the bonVito platform, giving it a valuable stream of recurring revenues.

Adoption of the bonVito software increased markedly in FY16, with the number of participating branches increasing 29% to 2,671, with five million bonVito cards in circulation. 2-3% of customers are now using bonVito.

## **Coca-Cola partnership expands addressable market**

In March 2017, Vectron announced a co-operation with Coca-Cola with the goal of forming the leading online marketing platform for the hospitality sector in German-speaking Europe. This initiative is based around Coca-Cola's GetHappy loyalty app – consumers can earn GetHappy points when spending at participating merchants. The GetHappy app was originally launched in 2015 and has been downloaded 350,000 times, with more than 10,000 participating companies. The second version of the app is currently under development and will be powered by technology derived from bonVito. The aim of the new version of the app is to provide more comprehensive functionality for merchants as well as integration with Vectron POS systems if used by the merchant. This initiative is expected to be formally launched in late 2017, at which point participating merchants will be able to offer and manage online orders and reservations via the app. The app will also offer functionality for automatic redemption of eCoupons, and making use of the bonVito platform, will enable targeted sales promotion campaigns and loyalty reward schemes. As an added attraction for consumers, GetHappy points will not only be redeemable for various products and services, but will also automatically entitle each points holder to participate in a regular sweepstake.

The services will be monetised via transaction charges, eg €0.99 fee per table booking, €0.5 fee for coupon redemption, 5% of value of orders placed. Vectron will be the recipient of the majority of the revenues, while Coca-Cola will benefit from the customer data.

This agreement is strategically important to Vectron, as it should diversify its revenue streams away from sales of POS hardware and software. Furthermore, like the bonVito app, revenues from the Coca-Cola partnership will be recurring in nature, which is beneficial for cash flow forecasting, valuation and the cost of capital, among other factors.

In our view, Vectron's downside exposure is limited, as Coca-Cola is absorbing the bulk of the sales and marketing costs within its own existing regional sales and marketing team of 750. However, should adoption of the app prove successful, then it would represent a significant revenue opportunity. Assuming revenues of €100 per month per restaurant (OpenTable earns c \$600 per month, Lieferando.de c €280 per month), for every percentage point of the German market share (approximately 210,000 eligible outlets) that Vectron gains, Vectron would receive recurring revenues of approximately €2.5m per annum. This excludes the further potential to cross-sell Vectron hardware to the companies that use GetHappy, but are not presently customers of Vectron POS systems. Should the launch in Germany prove successful, the scheme could be rolled out in additional geographies, representing further upside potential.

## Market overview

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Vectron is focused on the hospitality market, with no real presence in the retail market. The large POS system providers such as Ingenico, Verifone and NCR are much more focused on the retail market and hence are not competitors for Vectron. Instead, the company competes with many small, local POS system providers. With an installed base of 190,000 systems, of which c 100,000 are in Germany, management estimates it has a c 25% share of the hospitality sectors in Germany, Austria, and Benelux, and is in the top 10 of European POS system manufacturers.

In Germany, there are c 210,000 hospitality venues, of which only c 5% are chains. There are many businesses that have only one venue and they typically do not have the resources to manage complex IT. This has provided the opportunity for Vectron to specialise in serving this market, where it has developed a network of local resellers who are experienced in installing and supporting Vectron's technology.

The mPOS market was pioneered by Square, which developed a "dongle" that could be used to turn a smartphone or iPad into a card payment device – its service provides hardware and software to turn standard devices into POS devices as well as providing the merchant acquiring relationship. Other similar services rapidly followed, such as iZettle and Payleven in Europe. Square had recognised that small, start-up ventures often struggle to obtain acquiring services from traditional sources (banks or payment processors) and therefore developed a service that allowed these merchants to take card payments. Vectron's customer base tends to already have an acquiring relationship so its mPOS services concentrate on providing the software to make its customers' own hardware operate as POS devices.

In the online marketing space, companies tend to offer one specific service, such as table reservations, food delivery or loyalty schemes. Several of these services operate across Europe (see Exhibit 4).

Vectron's partnership with Coca-Cola is designed to provide a more comprehensive service to merchants, enabling them to use just one app to provide online table reservations, food ordering, loyalty schemes, and promotions, with the benefit of being integrated with Vectron's till systems. It has been designed to be cheaper than the alternatives. Coca-Cola has relationships with c 95% of hospitality merchants, which combined with Vectron's 25% share of the German market, gives the scheme good access to the hospitality market in Germany.



**Exhibit 4: Online services for the German hospitality industry**

Type of service	Owned by	Coverage	Scale
<b>Food ordering/delivery</b>			
DeliveryHero	Private	Europe, Middle-East, Latin America, Asia-Pacific, Africa	300,000 restaurants
Deliveroo	Private	Europe, Asia-Pacific	N/A
FoodPanda	Delivery Hero	Europe, Africa, Asia-Pacific	40,000 restaurants
JustEat	UK-listed	Europe, Asia-Pacific, Americas	69,500 restaurants
takeaway.com	Amsterdam-listed	Europe	28,000 restaurants
<b>Table reservations</b>			
Bookatable	Michelin	Europe, Americas	13,000 restaurants
LaForchette	TripAdvisor	Europe	12,000 restaurants
OpenTable	Priceline	Americas, Europe, Asia-Pacific	40,000 restaurants
Quandoo	Recruit Co., Ltd	Europe, Asia-Pacific	15,000 restaurants

Source: Company accounts

## Financials

**Exhibit 5: Financial summary**

€m, German GAAP			2012	2013	2014	2015	2016
Year end 31 December							
<b>Income statement</b>							
Revenue			22.67	21.41	22.42	25.87	33.72
EBITDA			1.77	1.51	1.56	2.64	3.61
EBITDA margin			7.8%	7.1%	7.0%	10.2%	10.7%
EBIT			0.88	0.96	1.02	2.07	3.08
EBIT margin			3.9%	4.5%	4.6%	8.0%	9.1%
Profit Before Tax (as reported)			0.97	1.03	1.08	1.83	2.96
Net income (as reported)			0.32	0.37	0.52	1.18	1.96
EPS (as reported) (€)			0.21	0.25	0.35	0.79	1.19
Dividend per share (€)			0.30	0.30	0.30	0.45	N/A
<b>Balance sheet</b>							
Total non-current assets			2.40	2.17	2.33	2.15	2.06
Total current assets			11.28	11.08	11.17	17.25	22.50
Total assets			13.69	13.25	13.50	19.40	24.56
Total current liabilities			(1.7)	(2.1)	(1.3)	(4.4)	(2.0)
Total non-current liabilities			(2.0)	(1.5)	(2.4)	(7.2)	(7.7)
Total liabilities			(3.7)	(3.6)	(3.7)	(11.7)	(9.7)
Net assets			10.03	9.68	9.75	7.72	14.87
Net debt/(cash)			0.4	0.1	(0.9)	(1.7)	(7.2)
<b>Cash flow</b>							
Net cash from operating activities			0.60	0.24	1.84	1.51	0.78
Net cash from investing activities			(1.1)	(0.4)	(0.3)	(0.4)	(0.4)
Net cash from financing activities			(2.0)	(0.4)	(0.6)	3.2	1.9
Net cash flow			(2.4)	(0.6)	1.0	4.3	2.2
Cash & cash equivalent end of year			4.70	4.13	5.11	9.46	11.67

Source: Vectron Systems accounts, Bloomberg

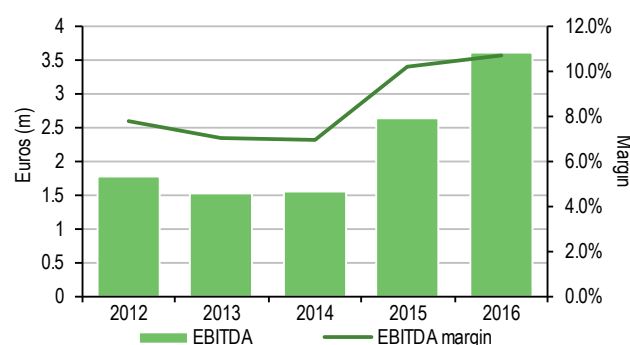
### Income statement

The company has grown revenues at a CAGR of 8.3% from FY12 to FY16, with the majority of this increase over the last two years. Management has successfully expanded margins, with CAGR for EBITDA and EPS of 15.4% and 41.5%, respectively, over the same period. Growth in FY15 and FY16 was helped by the introduction of the Duratec product as well as regulatory changes. We note that bonVito is not consolidated so its revenue contribution is not evident in these numbers.

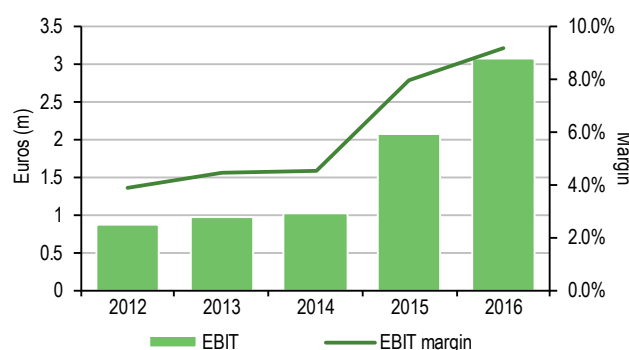
**Exhibit 6: Revenue split by geography and product type**

€m	Revenues					Revenue growth			
	2012	2013	2014	2015	2016	2013	2014	2015	2016
<b>POS systems</b>	<b>18.04</b>	<b>16.87</b>	<b>17.33</b>	<b>19.32</b>	<b>22.47</b>	<b>-6.5%</b>	<b>2.8%</b>	<b>11.5%</b>	<b>16.3%</b>
Germany	12.15	11.85	11.66	13.51	17.33	-2.5%	-1.7%	15.9%	28.3%
Other EU	5.35	4.37	5.25	5.33	4.81	-18.4%	20.3%	1.4%	-9.8%
International	0.53	0.64	0.43	0.48	0.32	21.6%	-33.9%	12.2%	-32.1%
<b>Software</b>	<b>1.49</b>	<b>1.46</b>	<b>2.02</b>	<b>2.58</b>	<b>2.33</b>	<b>-1.9%</b>	<b>37.6%</b>	<b>27.8%</b>	<b>-9.5%</b>
Germany	0.97	0.95	1.45	1.88	1.68	-1.7%	51.9%	30.0%	-10.8%
Other EU	0.48	0.44	0.50	0.61	0.61	-8.2%	14.9%	21.4%	0.8%
International	0.05	0.08	0.07	0.09	0.04	56.3%	-12.0%	28.8%	-52.9%
<b>Merchandise &amp; accessories</b>	<b>3.15</b>	<b>3.08</b>	<b>3.07</b>	<b>3.97</b>	<b>8.92</b>	<b>-2.1%</b>	<b>-0.3%</b>	<b>29.4%</b>	<b>124.6%</b>
Germany	2.37	2.25	2.42	3.26	6.85	-5.0%	7.4%	34.7%	110.1%
Other EU	0.76	0.79	0.63	0.69	1.97	3.6%	-20.0%	9.5%	186.2%
International	0.01	0.04	0.02	0.02	0.10	178.6%	-48.7%	10.0%	350.0%
<b>Total revenues</b>	<b>22.67</b>	<b>21.41</b>	<b>22.42</b>	<b>25.87</b>	<b>33.72</b>	<b>-5.6%</b>	<b>4.7%</b>	<b>15.4%</b>	<b>30.4%</b>

Source: Vectron Systems accounts

**Exhibit 7: EBITDA profitability**


Source: Vectron Systems

**Exhibit 8: EBIT profitability**


Source: Vectron Systems

## Strong momentum continues into Q117

The company reported Q117 revenue growth of 40% y-o-y to €10.6m, with regulation acting as a strong driver of demand. EBITDA of €1.97m (margin 18.5%) increased 155% y-o-y and EBIT of €1.84m (margin 17.3%) increased 190% y-o-y. Cash increased to €12.3m from €11.7m at year-end.

## Consensus forecasts reflect multiple outcomes

We summarise below consensus forecasts for Vectron Systems. This hides the wide range of forecasts; for example FY17 revenue forecasts range from €30.5m to €55.4m and EBITDA from €3.1m to €19.1m.

**Exhibit 9: Consensus forecasts**

€m	FY17e	FY18e
Revenues	42.5	52.2
EBITDA	9.3	13.0
EBIT	8.6	12.3
EPS (€)	3.48	5.21

Source: Bloomberg

With several growth drivers in the core business as well as the potential offered by the Coca-Cola partnership, it is clear that there are many possible outcomes. We show below several possible scenarios for the GetHappy scheme, and the potential impact it could have on operating profit and EPS forecasts.



**Exhibit 10: Scenario analysis for GetHappy app launch in Germany**

€m		FY18	FY19	FY20	FY21	FY22
Number of potential customers	210,000					
<b>Penetration</b>						
	Gain 1% pa	2,100	4,200	6,300	8,400	10,500
	Gain 5% pa	10,500	21,000	31,500	42,000	52,500
<b>Total revenue</b>						
Gain 1% pa	€100/venue/month	€2.5	€5.0	€7.6	€10.1	€12.6
Gain 5% pa	€100/venue/month	€12.6	€25.2	€37.8	€50.4	€63.0
<b>Vectron revenues</b>						
Gain 1% pa	75% retained	€1.89	€3.78	€5.67	€7.56	€9.45
Gain 5% pa	75% retained	€9.45	€18.90	€28.35	€37.80	€47.25
Gain 1% pa	95% retained	€2.39	€4.79	€7.18	€9.58	€11.97
Gain 5% pa	95% retained	€11.97	€23.94	€35.91	€47.88	€59.85
<b>Operating profit</b>						
Gain 1% pa, retain 75%	75% margin	€1.42	€2.84	€4.25	€5.67	€7.09
Gain 5% pa, retain 75%	75% margin	€7.09	€14.18	€21.26	€28.35	€35.44
Gain 1% pa, retain 95%	75% margin	€1.80	€3.59	€5.39	€7.18	€8.98
Gain 5% pa, retain 95%	75% margin	€8.98	€17.96	€26.93	€35.91	€44.89
<b>Post-tax contribution (@30% tax)</b>						
Gain 1% pa, retain 75%		€0.99	€1.98	€2.98	€3.97	€4.96
Gain 5% pa, retain 75%		€4.96	€9.92	€14.88	€19.85	€24.81
Gain 1% pa, retain 95%		€1.26	€2.51	€3.77	€5.03	€6.28
Gain 5% pa, retain 95%		€6.28	€12.57	€18.85	€25.14	€31.42
<b>Per share contribution (€)</b>						
Gain 1% pa, retain 75%		€0.60	€1.20	€1.80	€2.41	€3.01
Gain 5% pa, retain 75%		€3.01	€6.01	€9.02	€12.03	€15.03
Gain 1% pa, retain 95%		€0.76	€1.52	€2.29	€3.05	€3.81
Gain 5% pa, retain 95%		€3.81	€7.62	€11.43	€15.23	€19.04

Source: Edison Investment Research

## Balance sheet and cash flow

As the company outsources the manufacturing of components and sub-assemblies, it has limited capex requirements. Over the last five years, capex has ranged between 1.3% and 3.2% of sales. The company does not capitalise software development costs.

In 2012, the company invested €500k to set up bonVito and in 2014 forgave €400k in receivables, bringing its investment to €900k to date. At the end of FY16, bonVito was recorded on the balance sheet at a value of €164k (€900k investment less €749k losses to date). In FY16, bonVito generated a net loss of €118k and management believes it should soon reach break-even.

The company moved from a net debt position to a net cash position in 2014 and issued 150,000 shares in H116, raising funds of €5.9m. Net debt at the end of 2016 was made up of gross cash of €11.7m, €2.9m in bank loans (being repaid at €0.84m per annum) and a further €1.5m due in mezzanine financing (due for repayment in February 2019).

We note that the company offers a leasing scheme to its customers. Vectron sells the hardware to a leasing company and leases it back; in turn, it leases the hardware to the customer. Neither the lease receivables or payables are recorded on the balance sheet – we understand they amounted to c €4m at the end of FY16.

## Valuation

The stock has performed exceptionally well over the last three years, with growth of 37% in 2014, 193% in 2015, 110% in 2016 and 100% year-to-date. In our view, this reflects multiple growth drivers helping the core business plus the potential upside from the GetHappy scheme.

**Exhibit 11: Share price performance over three years**



Source: Bloomberg

**Exhibit 12: Share price performance over one year**



Source: Bloomberg

## Peer valuation

Exhibit 13 shows Vectron's valuation versus a range of peers, from smaller domestic based POS operators to significantly larger international companies. Vectron currently trades on an FY17 EV/sales ratio of 4.7x, against a median of 2.2x, and an EV/EBITDA of 21.3x, versus the peer median of 9x. With revenues forecast to grow 26% in FY17 and 23% in FY18, driving EBITDA margins above the peer group average, in our view the share price is factoring in substantial growth in the core business as well as some level of success with the GetHappy initiative.

**Exhibit 13: Peer valuation multiples**

Company	Quoted ccy	Share price	Market cap (m)	EV (reporting ccy -m)	EV/sales (x)		EV/EBITDA (x)		P/E (x)		Div yield		EBITDA margin	
					CY	NY	CY	NY	CY	NY	CY	NY	CY	NY
<b>VECTRON SYSTEMS</b>	€	124.45	205	198	4.7	3.8	21.3	15.3	35.7	23.9	0.3%	0.3%	21.8%	24.9%
<b>Large POS providers</b>														
INGENICO GROUP	€	87.15	5358	5498	2.2	2.0	10.8	9.8	18.5	16.6	1.8%	2.1%	20.4%	20.8%
NCR CORPORATION	US\$	39.4	4776	8518	1.3	1.2	7.5	7.2	11.7	10.8			17.0%	17.2%
VERIFONE SYSTEMS	US\$	17.5	1951	2746	1.4	1.4	9.0	8.1	12.7	10.6	0.0%		15.9%	17.0%
<b>Small/mid-cap POS providers</b>														
AURES TECHNOLOGIES	€	25.3	101	96	1.2	1.1	8.8	7.8	13.9	12.3	2.2%	2.4%	13.2%	13.7%
PAYPOINT PLC	£	1009.0	687	638	4.7	4.8	10.8	10.4	16.4	15.5	0.1%	0.1%	43.5%	46.3%
UNIVERSE GROUP	£	10.5	24	22	1.0	0.9	5.3	4.9	11.7	10.5			19.1%	19.3%
PAX GLOBAL TECHNOLOGY LTD	HK\$	4.7	5221	3049	0.9	0.8	4.3	3.8	8.3	7.4	1.7%	1.8%	22.0%	22.0%
<b>mPOS provider</b>														
SQUARE INC - A	US\$	19.9	7448	6907	7.5	5.8	56.2	31.9	93.9	54.8	0.0%	0.0%	13.4%	18.3%
<b>Online service providers</b>														
JUST EAT PLC	£	600.0	4074	3952	8.0	6.6	24.4	18.3	35.7	25.8	0.0%	0.0%	32.7%	36.0%
GRUBHUB INC	US\$	43.4	3739	3377	5.2	4.2	18.5	14.6	39.5	31.8	0.0%	0.0%	28.0%	28.9%
TAKEAWAY.COM HOLDING BV	€	32.7	1414	1279	8.1	6.1		70.7		150.3			(6.0)%	8.7%
RETAILMENOT INC	US\$	11.6	560	394	1.3	1.2	6.8	6.6	21.2	20.7			18.6%	18.2%
EAGLE EYE SOLUTIONS GROUP	£	241.0	54	54	5.0	3.5		35.8					(11.6)%	9.8%
<b>Average</b>					<b>3.7</b>	<b>3.1</b>	<b>14.8</b>	<b>17.7</b>	<b>25.8</b>	<b>30.6</b>	<b>0.7%</b>	<b>0.9%</b>	<b>17.4%</b>	<b>21.2%</b>
<b>Median</b>					<b>2.2</b>	<b>2.0</b>	<b>9.0</b>	<b>9.8</b>	<b>16.4</b>	<b>16.0</b>	<b>0.0%</b>	<b>0.1%</b>	<b>18.6%</b>	<b>18.3%</b>

Source: Bloomberg. Note: Prices as at 22 May 2017.

## Management, organisation and corporate governance

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### Supervisory board and management board

In keeping with other German companies, Vectron has a two-tier board structure in which the executive board is overseen by a separate supervisory board. The executive board consists of founders Mr Jens Reckendorf, who is the managing director for business technology and development, and Mr Thomas Stümmeler, who is the managing director for the finance, marketing and sales divisions of the business.

There are three members of the supervisory board: Mr Christian Ehlers (chairman), Mr Maurice Oosenbrugh (vice chair) and Mr Heinz-Jürgen Buss (NED).

### Shareholders and free float

Senior management Jens Reckendorf (28.1%) and Thomas Stümmeler (28%) hold a combined 56% of the total share capital of the company, leaving a free float of 44%. Other significant shareholders include the Massachusetts Mutual Life Insurance Company (4.5%) and Montagu Private Equity (3.1%).

## Sensitivities

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Vectron's financial performance and share price will be sensitive to the following factors:

- **Exposure to Germany:** with 77% of revenues generated in Germany, the health of the German economy will have a material influence on the performance of the company.
- **Currency:** as revenues become more international the relative strength of the euro will become increasingly important.
- **Technical enhancements:** usage of mobile consumer hardware (smartphones, tablets, etc) may encroach on traditional POS system demand.
- **Competition:** the efficacy and pricing of Vectron's product offering relative to its peers will influence demand for the company's solutions.
- **Regulatory issues:** Vectron is currently benefiting from changes to electronic cash register legislation. The size and timing of this boost to revenues is uncertain.
- **Free float:** management owns 56% of the company.
- **Uptake of GetHappy app:** the pace and level of adoption of the GetHappy app by merchants and consumers is difficult to predict.

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