EDISON

Osirium Technologies

FY19 results

Reflecting COVID-19 risk to bookings

Software & comp services

Osirium's FY19 results were broadly in line with forecasts. The company saw strong bookings growth in FY19 from a combination of new customers, renewals and expansion of existing contracts. The product suite was expanded to include privileged process automation and privileged endpoint management solutions. While COVID-19 disruption has not yet had a noticeable impact on demand, we are taking a more cautious approach to our bookings and revenue forecasts for FY20 before factoring in a reacceleration of growth in FY21.

Year end	Revenue (£m)	EBITDA* (£m)	EPS* (p)	DPS (p)	P/E (x)	EV/Sales (x)
12/18	0.96	(1.77)	(18.1)	0.0	N/A	3.6
12/19	1.17	(2.15)	(19.5)	0.0	N/A	3.0
12/20e	1.52	(2.01)	(17.4)	0.0	N/A	2.3
12/21e	2.10	(1.62)	(16.3)	0.0	N/A	1.7

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

FY19 results broadly in line

FY19 bookings and revenues were broadly in line with the January trading update: bookings grew 54% y-o-y while a growing number of multi-year deals means that reported revenue grew 22% y-o-y. Due to the first time introduction of IFRS 16 and higher than forecast capitalised development costs, EBITDA was £222k ahead of our -€2.37m forecast. An operating loss of £3.98m was in line with our forecast. Net loss of £2.83m (our estimate £2.86m) benefited from a higher than forecast tax credit. Gross cash was £3.9m at the end of FY19, with net cash at £1.5m.

Factoring in some caution in FY20

With the number of people working from home substantially higher y-o-y and likely to remain high even once COVID-19 disruption has passed, the security of both administrator accounts and end-devices will be more important than ever. However, in the short term, although Osirium has not yet seen evidence of this, we believe some customers may delay investment decisions, and we have reduced our FY20 bookings and revenue forecasts accordingly. We expect demand to be robust once the economy moves to a normal footing. Our FY20 operating loss forecast increase by 3.8% to £3.78m and we introduce an FY21 operating loss forecast of £3.54m.

Valuation: Bookings the key driver

Osirium is trading at a discount to peers on an EV/Sales basis. As it is an early-stage company several years from profitability, we have performed a reverse DCF to analyse the assumptions factored into the current share price, using a WACC of 10% and a terminal growth rate of 3%. We estimate that the current share price is discounting average bookings growth of 19% for FY22–29e, break-even EBITDA in FY24, average EBITDA margins of 7.5% for FY22–29e and a terminal EBITDA margin of 30%. In our view, bookings growth is the key driver of share price performance.

19 May 2020

Price	**25.5p**
Market cap	**£5m**

Net cash (£m) at end FY19	1.5
Shares in issue	19.5m
Free float	91%
Code	OSI
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(23.9)	10.9	(67.1)
Rel (local)	(26.9)	37.5	(60.1)
52-week high/low		90p	17p

Business description

UK-based Osirium Technologies designs and supplies subscription-based cybersecurity software. Its PAM platform includes privileged access, task, session and behaviour management. It recently launched a secure process automation solution (PPA) and a privileged endpoint management (PEM) solution.

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Osirium Technologies is a research client of Edison Investment Research Limited

Review of FY19 results

Exhibit 1: Osirium FY19 results highlights

£'000s	FY18a	FY19e	FY19a	Diff	y-o-y
Bookings	1,177.3	1,801.3	1,815.8	0.8%	54.2%
Revenues	957.5	1,149.7	1,171.6	1.9%	22.4%
EBITDA	(1,767.3)	(2,374.4)	(2,152.1)	(9.4%)	21.8%
EBITDA margin	-184.6%	-206.5%	-183.7%	(11.1%)	
Normalised/reported operating profit	(2,674.8)	(3,388.0)	(3,399.7)	0.3%	27.1%
Normalised/reported operating margin	-279.4%	-294.7%	-290.2%	4.5%	
Normalised/reported PBT	(2,675.4)	(3,425.8)	(3,451.9)	0.8%	29.0%
Normalised/reported net income	(2,267.8)	(2,857.1)	(2,829.4)	(1.0%)	24.8%
Normalised/reported basic EPS (p)	(18.14)	(19.49)	(19.45)	(0.2%)	7.2%
Gross cash		3,857.0	3,854.9	(0.1%)	
Net debt/(cash)	(2,386.6)	(1,119.2)	(1,509.5)	34.9%	(36.8%)

Source: Osirium, Edison Investment Research

Osirium reported revenues and bookings substantially in line with the January trading update (revenues >£1.1m, bookings >£1.8m). Due to the number of multi-year deals signed in FY19, bookings growth exceeded revenue growth. Deferred income at the end of FY19 stood at £1.37m, 89% higher than a year ago. The company noted that it had a 100% subscription renewal rate in FY19.

EBITDA of -£2.15m was better than our forecast of -£2.37m. While operating costs were £200k lower than forecast, we estimate that c £50k of this was due to the first time application of IFRS 16, which removed lease costs, and the remainder was due to higher than expected capitalisation of development costs (£1.77m versus our £1.60m forecast). At the operating profit level, the difference was minimal, due to the £49k first-time depreciation of right-of-use assets and higher than expected amortisation (£1.14m versus our £963k forecast).

The company reported a tax credit of £623k (effective rate 18%), higher than our £569m forecast (effective rate 17%). Of this, £557m was an R&D tax credit and the remainder was a prior year adjustment. Overall, the reported net loss was 1% smaller than we had forecast.

Gross cash at year-end of £3.85m was substantially in line with our forecast. Net cash was better than forecast, as the company accounted for the convertible debt issued in October 2019 as a mixture of debt and equity, whereas we had treated it wholly as debt.

Business update

COVID-19: Increases risk, but no material impact yet

In its April update, the company noted that staff were working from home and continuing to support customers remotely. While it has become more difficult to build the new business pipeline through face-to-face activity such as conferences, the company has shifted its marketing and sales activity to make more use of digital channels. The company is closely controlling its cost base and will adapt accordingly.

Expanding the product portfolio

During FY19, the company launched two new products: Privileged Process Automation (PPA) in Q2 and Privileged Endpoint Manager (PEM) in Q4 and recorded its first PPA sale with an existing customer. Since year-end, the company has released v7.0 of its PAM platform, which introduces the concept of clustering. The company has developed the ability to cluster instances of Osirium servers together (‘mesh’) to ensure high availability. This means that a much higher number of devices can be managed by an installed instance. The goal is that the servers should be able to communicate with each other to enforce the rule that there is only one instance of an ID at any one time. This should also provide fault tolerance, with the ability to reconfigure the mesh in the event of any of the clustered servers failing.

The focus of R&D during FY20 will be the ongoing refinement of the platform’s technical specifications and user interface. The aim is to add new functionality and capabilities to the three core offerings, and the company will be exploring an offering targeted at managed service providers.

In January, the company signed a technology partnership with TSplus, a provider of remote access and application delivery solutions. TSplus technology is being used as a core component of the Osirium MAP Server, expanding the range of applications, devices and users that can benefit from Osirium’s privileged access management capabilities.

Growing the customer base

During FY19, the company added new customers in existing verticals (finance, NHS) and added customers in new verticals (fleet management services, central government). Since the year-end, the company has made further sales to the NHS and Ambulance Services. Customers totalled 50 at year-end, up from 36 at the end of FY18. During the year, the company saw fewer customers needing to undertake a proof of concept (POC) before signing up. Of those POCs that did happen in the year, 100% were converted to a sale.

Several contracts signed in FY19 were via channel partners including system integrators, managed service providers and managed security service providers. The company continues to build its channel partner relationships.

With 100% of contracts up for renewal in FY19 being renewed, the company also saw a number of customers increase the number of devices protected.

Post year-end, the company established a presence in Benelux and started sales and marketing activities in Benelux and the Nordics.

Outlook and changes to estimates

We have revised our FY20 forecasts to reflect FY19 results and have made the following changes:

- **Bookings:** we have taken a more cautious approach as we assume that despite the obvious need for its technology, potential customers will be controlling their own cost bases more closely during the COVID-19 disruption and may delay making investment decisions.
- **Revenues:** these are a function of bookings intake, so we have reduced our FY20 forecast. We introduce a forecast for 38% growth in FY21.
- **Costs:** we factor in a slightly slower increase in headcount over the year. We also reflect IFRS 16 for the first time. Overall, we are factoring in slightly lower operating costs, slightly higher capitalised development costs and related amortisation, and depreciation of right-of-use assets.
- **Cash:** we forecast a gross cash position of £0.93m by the end of FY20. We expect that the company will need to seek new financing in FY21 – we have modelled debt financing of £2.5m. If the company achieves faster bookings growth than we forecast, this will reduce the future funding requirement.

Exhibit 2: Changes to forecasts

£'k	FY20e	FY20e			FY21e	
	Old	New	Change	y-o-y	New	y-o-y
Bookings	2,341.6	2,179.0	(6.9%)	20.0%	2,941.6	35.0%
Revenues	1,882.7	1,521.5	(19.2%)	29.9%	2,096.2	37.8%
EBITDA	(2,375.1)	(2,222.8)	(6.4%)	3.3%	(1,783.9)	(19.7%)
EBITDA margin	-126.2%	-146.1%	15.8%		-85.1%	
Normalised operating profit	(3,635.9)	(3,775.1)	3.8%	11.0%	(3,540.4)	(6.2%)
Normalised operating margin	-193.1%	-248.1%	(55.0%)		-168.9%	
Reported operating profit	(3,635.9)	(3,775.1)	3.8%	11.0%	(3,540.4)	(6.2%)
Reported operating margin	-193.1%	-248.1%	(55.0%)		-168.9%	
Normalised PBT	(3,838.4)	(3,979.7)	3.7%	15.3%	(3,745.0)	(5.9%)
Reported PBT	(3,838.4)	(3,979.7)	3.7%	15.3%	(3,745.0)	(5.9%)
Normalised net income	(3,262.6)	(3,382.7)	3.7%	19.6%	(3,183.3)	(5.9%)
Reported net income	(3,262.6)	(3,382.7)	3.7%	19.6%	(3,183.3)	(5.9%)
Normalised basic EPS (p)	(16.74)	(17.35)	3.7%	(10.8%)	(16.33)	(5.9%)
Normalised diluted EPS (p)	(16.74)	(17.35)	3.7%	(10.8%)	(16.33)	(5.9%)
Reported basic EPS (p)	(16.74)	(17.35)	3.7%	(10.8%)	(16.33)	(5.9%)
Gross cash	646.1	930.7	44.0%		901.3	
Net debt/(cash)	2,294.1	1,617.2	(29.5%)	(207.1%)	4,349.1	168.9%

Source: Edison Investment Research

Valuation

The share price is essentially flat year to date, declining with the market in March to a low of 17p, then rebounding through April to reach a high of 39p before returning to the current level. Compared to cybersecurity peers trading on an average EV/Sales multiple of 4.6x this year's revenues and 4.2x next year, Osirium is trading at a discount (FY20e 2.3x, FY21e 1.7x). In our view, the key factor to trigger upside will be evidence that bookings have not been materially negatively affected by COVID-19.

As we do not expect Osirium to reach profitability within our explicit forecast period, we use a reverse discounted cash flow analysis to calculate the assumptions underlying the current share price. With a WACC of 10% and a terminal growth rate of 3%, we arrive at the current share price using the following assumptions for the period after our 2020–21 explicit forecasts:

- Bookings growth of 25% per year in 2022 and 2023, reducing every year thereafter to 15% by 2028, with 28% recognition in the year invoiced and 65% of deferred income unwinding each year.
- Revenue growth: trending down from 32% in 2022 to 15% in 2029.
- EBITDA margin: hitting break-even EBITDA in 2024, rising to 30% margin by 2029. This assumes the company continues to capitalise development costs at a similar rate over the period of the analysis. We note that this equates to a terminal EBIT margin of 5.9%, well below established software vendors.
- Working capital: negative working capital requirements due to the upfront payment subscription model.
- Capex (mainly capitalised development costs): we forecast this to reduce from 72% of sales in 2022 to 24% by 2029.

Exhibit 3: Financial summary

£'k	2013	2014	2015	2016	2017	2018	2019	2020e	2021e
31-December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT									
Revenue	120.0	207.0	290.2	477.6	647.6	957.5	1,171.6	1,521.5	2,096.2
EBITDA	(366.7)	(327.1)	(377.9)	(1,136.7)	(1,609.4)	(1,767.3)	(2,152.1)	(2,222.8)	(1,783.9)
Normalised operating profit	(679.4)	(714.3)	(790.7)	(1,725.6)	(2,296.8)	(2,674.8)	(3,399.7)	(3,775.1)	(3,540.4)
Amortisation of acquired intangibles	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Share-based payments	0.0	(184.3)	(56.4)	(96.9)	0.0	0.0	0.0	0.0	0.0
Reported operating profit	(679.4)	(898.5)	(847.1)	(1,822.5)	(2,296.8)	(2,674.8)	(3,399.7)	(3,775.1)	(3,540.4)
Net Interest	(35.2)	5.7	(9.9)	9.7	4.2	(0.6)	(52.2)	(204.6)	(204.6)
Joint ventures & associates (post tax)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Profit Before Tax (norm)	(714.6)	(708.5)	(800.7)	(1,715.9)	(2,292.6)	(2,675.4)	(3,451.9)	(3,979.7)	(3,745.0)
Profit Before Tax (reported)	(714.6)	(892.8)	(857.1)	(1,812.8)	(2,292.6)	(2,675.4)	(3,451.9)	(3,979.7)	(3,745.0)
Reported tax	137.7	134.1	121.0	453.3	409.4	407.6	622.5	597.0	561.8
Profit After Tax (norm)	(576.9)	(602.1)	(687.6)	(1,286.9)	(1,883.2)	(2,267.8)	(2,829.4)	(3,382.7)	(3,183.3)
Profit After Tax (reported)	(576.9)	(758.7)	(736.0)	(1,359.6)	(1,883.2)	(2,267.8)	(2,829.4)	(3,382.7)	(3,183.3)
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net income (normalised)	(576.9)	(602.1)	(687.6)	(1,286.9)	(1,883.2)	(2,267.8)	(2,829.4)	(3,382.7)	(3,183.3)
Net income (reported)	(576.9)	(758.7)	(736.0)	(1,359.6)	(1,883.2)	(2,267.8)	(2,829.4)	(3,382.7)	(3,183.3)
Basic ave. number of shares outstanding (m)	0	1	10	10	10	13	15	19	19
EPS - normalised (p)	N/A	N/A	(6.61)	(12.38)	(18.12)	(18.14)	(19.45)	(17.35)	(16.33)
EPS - normalised fully diluted (p)	N/A	N/A	(6.61)	(12.38)	(18.12)	(18.14)	(19.45)	(17.35)	(16.33)
EPS - basic reported (p)	(296.36)	(144.92)	(7.08)	(13.08)	(18.12)	(18.14)	(19.45)	(17.35)	(16.33)
Dividend (p)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Revenue growth (%)	26.3	72.6	40.2	64.6	35.6	47.9	22.4	29.9	37.8
EBITDA Margin (%)	-305.7	-158.0	-130.2	-238.0	-248.5	-184.6	-183.7	-146.1	-85.1
Normalised Operating Margin	-566.3	-345.0	-272.5	-361.3	-354.7	-279.4	-290.2	-248.1	-168.9
BALANCE SHEET									
Fixed Assets	815.7	805.2	799.7	1,178.8	1,812.1	2,360.2	3,124.4	3,469.2	3,647.0
Intangible Assets	808.6	795.7	793.3	1,134.5	1,731.9	2,307.2	2,936.5	3,349.7	3,595.9
Tangible Assets	7.2	9.5	6.4	44.3	80.2	52.9	187.9	119.5	51.0
Investments & other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current Assets	109.3	269.2	428.1	3,953.7	1,646.4	3,134.6	4,837.3	2,031.1	2,206.4
Stocks	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debtors	77.2	218.6	154.6	380.9	622.6	748.0	982.4	1,100.4	1,305.0
Cash & cash equivalents	32.2	50.6	273.5	3,572.8	1,023.8	2,386.6	3,854.9	930.7	901.3
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current Liabilities	(235.2)	(294.2)	(365.0)	(648.5)	(857.7)	(1,170.3)	(1,923.0)	(2,675.7)	(3,543.5)
Creditors	(235.2)	(294.2)	(365.0)	(648.5)	(857.7)	(1,170.3)	(1,889.1)	(2,641.8)	(3,509.6)
Tax and social security	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Short term borrowings	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	(33.9)	(33.9)	(33.9)
Long Term Liabilities	(952.5)	(487.6)	(163.3)	0.0	0.0	0.0	(2,422.4)	(2,591.0)	(5,259.5)
Long term borrowings	(789.0)	(323.7)	0.0	0.0	0.0	0.0	(2,345.4)	(2,547.9)	(5,250.4)
Other long term liabilities	(163.4)	(163.9)	(163.3)	0.0	0.0	0.0	(77.0)	(43.1)	(9.1)
Net Assets	(262.6)	292.6	699.5	4,483.9	2,600.8	4,324.5	3,616.3	233.5	(2,949.7)
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Shareholders' equity	(262.6)	292.6	699.5	4,483.9	2,600.8	4,324.5	3,616.3	233.5	(2,949.7)
CASH FLOW									
Op Cash Flow before WC and tax	(366.7)	(327.1)	(377.9)	(1,136.7)	(1,609.4)	(1,767.3)	(2,152.1)	(2,222.8)	(1,783.9)
Working capital	66.3	3.8	120.7	226.8	85.5	187.2	633.7	634.7	663.1
Exceptional & other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tax	109.8	48.4	134.6	120.4	291.4	407.6	473.3	597.0	561.8
Net operating cash flow	(190.6)	(274.9)	(122.6)	(789.4)	(1,232.5)	(1,172.5)	(1,045.1)	(991.1)	(559.0)
Capex	(412.8)	(376.7)	(407.3)	(968.0)	(1,320.6)	(1,455.7)	(1,852.8)	(1,897.1)	(1,934.3)
Acquisitions/disposals	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.0	0.0
Net interest	(35.2)	5.7	(9.9)	9.7	4.2	(0.6)	0.0	0.0	0.0
Equity financing	0.0	639.3	762.8	5,047.1	0.0	3,991.5	1,726.4	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	(60.6)	(36.0)	(36.0)
Net Cash Flow	(638.6)	(6.5)	222.9	3,299.3	(2,549.0)	1,362.8	(1,231.7)	(2,924.2)	(2,529.4)
Opening net (cash)/debt	118.3	756.9	273.1	(273.5)	(3,572.8)	(1,023.8)	(2,386.6)	(1,509.5)	1,617.2
FX	0.0	0.0	0.0	0.0	0.0	0.0	(0.0)	(0.0)	0.0
Other non-cash movements	0.0	490.3	323.8	0.0	0.0	(0.0)	354.6	(202.5)	(202.5)
Closing net (cash)/debt	756.9	273.1	(273.5)	(3,572.8)	(1,023.8)	(2,386.6)	(1,509.5)	1,617.2	4,349.1

Source: Osirium, Edison Investment Research

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