

## DATAGROUP

**IT services**
**5 February 2019**

### Growth continues apace

DATAGROUP recorded another strong year of growth with revenue increasing by 22%, including 3.3% organic growth, or 6% when adjusting for discontinued activities from acquisitions. The recent acquisitions of ikb Data, HanseCom and ALMATO all performed well. During the year the group won its largest ever contract worth high double-digit million euros. This deal, with NRW Bank, was only attainable due to the ikb Data acquisition. With the shares having drifted back c 25% over the last year the rating looks increasingly attractive at c 8x EBITDA.

### Consolidating a fragmented IT services market

DATAGROUP is consolidating the highly fragmented German IT services market, focusing on Mittelstand companies with revenues of €100m to €1bn. This involves both buy-and-build and buy-and-turnaround approaches, transitioning the acquired businesses to DATAGROUP's more effective business model. DATAGROUP's CORBOX solutions are cloud-based, focused on fixed-price contracts, based on standardised processes that are certified according to ISO 20000 and backed by service level agreements (SLAs). DATAGROUP believes there is a huge opportunity in the Mittelstand space as these companies typically rely on their own expensive in-house IT departments and have difficulty adapting to new technologies. The broad range of services allows customers to fully outsource their IT operations. Much of the work is done remotely and the group can scale its data centre services and shared services desk to support a large number of customers.

### FY18 results: Underlying organic growth was 6%

Revenue grew by 21.9% to €272.1m and EBITDA rose 27% as margins expanded from 12.1% to 12.7%. The company signed 20 new CORBOX customers during the period and significantly extended business with 14 existing customers. The group ended FY18 with net debt of €12.1m, up from €4.1m a year earlier.

### Valuation: Increasingly attractive after the drift back

DATAGROUP offers an excellent track record, high recurring revenues, a clear focus on the large German Mittelstand sector and an increasing number of key differentiators following the acquisitions of ikb Data and ALMATO. The shares look increasingly attractive trading on c 17.5x FY20e earnings and c 8x EBITDA, given an outlook underpinned by a favourable business model supported by attractive business drivers, which also provide a compelling case for acquisitions.

#### Consensus estimates

Year end	Revenue (€m)	EBITDA (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
09/17	223.1	27.0	1.41	0.45	24.8	1.3
09/18	272.1	34.5	1.55	0.60	22.6	1.7
09/19e	283.3	36.3	1.66	0.55	21.1	1.6
09/20e	297.1	38.5	2.00	0.60	17.5	1.7

Source: Refinitiv

**Price** €35  
**Market cap** €292m

#### Share price graph



#### Share details

Code	D6H
Listing	Deutsche Börse Scale
Shares in issue	8.349m
Last reported net debt at 30 September 2018	€12.1m

#### Business description

DATAGROUP is a full IT outsourcing provider, focused on the German Mittelstand market. The company offers the full range of IT services on a modular basis, through its CORBOX 'cloud-enabling platform'. Services include service desk, end-user services, data centre services, application management and SAP services.

#### Bull

- A compelling growth strategy, scaling the business across the Mittelstand sector.
- Cloud services business model gives it a clear advantage over competitors.
- Centralised SLA-based approach with a focus on customer satisfaction puts company in a strong position to consolidate a fragmented market.

#### Bear

- Highly exposed to the German economy.
- Acquisitions bring risks, but DATAGROUP has a proven track record in integrating acquisitions.
- Increased debt levels, but the group is still well within its covenants.

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## FY18 results: Underlying organic growth of 6% excluding companies in transformation

Group revenue grew by 21.9% to €272.1m, boosted by the acquisitions of ikb Data, HanseCom and ALMATO. Organic growth was 3.2%; this rises to 6% when excluding the impact of discontinued businesses from acquisitions ie DATAGROUP sheds unprofitable business after making acquisitions and there is an ongoing managed decline in business from Hewlett Packard Enterprise relating to the acquisition of SAP and application management services from 2016. Recurring revenues jumped by 27% to €199m, representing 73% of the total, up from 70% a year earlier and 88% of gross profit was generated from these recurring revenues. Personnel expenses represented 49.5% of group revenue, which was 420bp lower than the prior year, Consequently, EBITDA jumped by 27.4% to €34.5m, with the margin rising by 60bp to 12.7%. The company is recommending an increase in the dividend by a third to 60c.

DATAGROUP signed 20 new CORBOX customers during the period, taking the total number of CORBOX customers to 150, and the company significantly extended business with 14 existing customers. The ikb Data acquisition created a new vertical in financial services, which would otherwise have been difficult to build as application management skills in financial services are very specialised. Ikb Data lost one client (ikb Leasing) but signed three more, including the record NRW.Bank deal worth high double-digit million euros, along with Bankhaus Lampe and BayernInvest. The contract with IKB Deutsche Industriebank, which sold the ikb Data business to DATAGROUP in 2017, is up for renegotiation shortly. HanseCom has been successfully reorganised and renamed Operate IT. ALMATO is proving to be value accretive and adds useful skills in the productivity enhancing robotic process automation (RPA) space.

### Exhibit 1: Financial summary

€000s	FY12	FY13	FY14	FY15	FY16	FY17	FY18
Year ended 30 September	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
Income statement (€000s)							
Revenue	146,183	156,935	152,380	157,574	174,918	223,142	272,100
Services & maintenance revenue	102,980	116,082	114,413	120,773	135,907	180,631	220,085
% group revenue	70%	74%	75%	77%	78%	81%	81%
Trade revenue	42,923	40,541	37,707	36,592	38,821	42,297	51,770
Other/consolidation	280	312	260	209	190	214	245
EBITDA	9,549	12,553	11,686	15,339	19,103	27,041	34,463
EBITDA margin	6.5%	8.0%	7.7%	9.7%	10.9%	12.1%	12.7%
EBIT	3,792	6,091	6,213	9,604	12,675	18,590	20,423
EPS	0.37	0.25	0.14	0.65	0.75	1.41	1.55
DPS	0.20	0.20	0.20	0.25	0.30	0.45	0.60
Balance Sheet (€000s)							
Total non current assets	69,647	66,109	60,754	68,062	92,178	102,864	114,448
Total current assets	31,019	35,590	34,345	35,285	67,568	110,526	101,002
Total assets	100,666	101,699	95,099	103,346	159,746	213,390	215,450
Total non-current liabilities	(32,416)	(49,420)	(44,056)	(39,013)	(97,367)	(95,881)	(86,707)
Total current liabilities	(45,552)	(29,767)	(29,778)	(40,283)	(34,012)	(57,928)	(61,488)
Total liabilities	(77,968)	(79,188)	(73,834)	(79,296)	(131,379)	(153,809)	(148,195)
Net Assets	22,698	22,511	21,264	24,051	28,367	59,581	67,255
Cash flow							
Net cash from operating activities	8,456	10,947	9,286	9,431	9,518	32,477	18,990
Net cash from investing activities	(17,950)	(5,210)	(4,301)	(9,295)	(3,711)	(19,749)	(19,104)
Net Cash from financing activities	12,056	2,778	(6,937)	(7,513)	16,545	16,027	(14,365)
Net Cash Flow	2,562	8,516	(1,951)	(7,375)	22,352	28,755	(14,479)
Cash & cash equivalent end of year	2,883	11,398	9,448	2,072	24,424	53,179	37,800

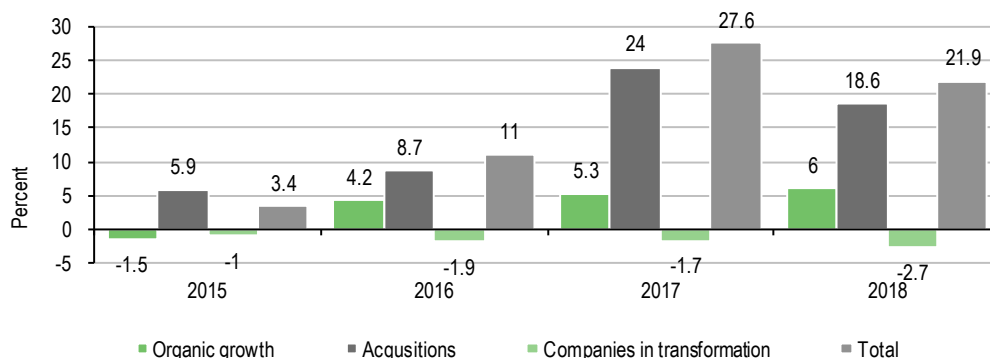
Source: Company accounts

Operating cash flow dipped by 42% to €19.0m, mainly due to a big swing in working capital reflecting the extraordinary high cash conversion in the prior year. According to DATAGROUP, after stripping out one-off effects, underlying operating cash flow actually rose from €20.6m to €21.7m. Capex increased by 42% to €14.8m, largely reflecting heavy investment in datacentre hardware

and infrastructure as well as operating and business equipment, and after a small amount of fixed asset disposals and net interest paid, free cash flow fell to €4.7m from €22.4m. After acquisition expenditure, dividends and interest, net debt, including acquisition liabilities, rose by €8.0m to €12.1m (using Datagroup's net debt definition).

The group generated 6% organic growth, excluding companies in transformation (mostly discontinued unprofitable contracts from acquisitions) which deducted 2.7%. Consequently, total organic growth was 3.3%. These numbers compare favourably with industry growth rates of 2.6% in Germany (Bitkom, February 2018). Acquisitions contributed 18.6% to the growth, taking total group revenue growth to 21.9%.

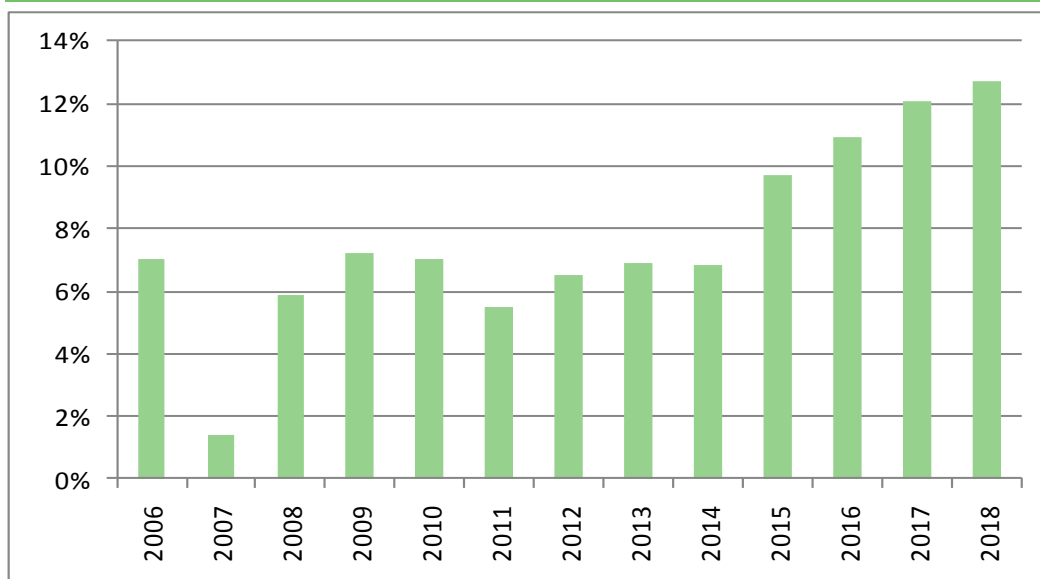
**Exhibit 2: Growth rates**



Source: Company accounts

As is standard company practice, no FY19 guidance has yet been given and management will update guidance at the time of the AGM. However, the group has an ambition to generate revenues of c €750m in 2025, including acquisitions. It also aspires to a long-term EBITDA margin of 13%, which we suspect could be increased given that the target is already almost met, and there are a number of drivers that could take margins higher, including utilising ALMATO's artificial intelligence expertise to automate group processes.

**Exhibit 3: EBITDA margins continue to rise**



Source: Company accounts

## **Expanded management board**

In October, Andreas Baresel took on the role of chief production officer (CPO), responsible for the overall management of the individual service factories within the group. Mr Baresel was previously managing director of DATAGROUP Business Solutions, the largest DATAGROUP company, where he has worked as a director since 2012. He was responsible for the development and expansion of the IT service business in Southern Germany. The promotion means three people now sit on the management board: CEO Max H.-H. Schaber, COO Dirk Peters and CPO Andreas Baresel.

## **Acquisition strategy**

The group has made 21 acquisitions since its IPO in 2006, with the last in January 2018 (ALMATO). Activity has slowed, as the market is not as attractive following a rise in valuations. Nevertheless, DATAGROUP is maintaining its acquisition strategy, which is to make infill acquisitions on regions where it is underrepresented in Germany, or to increase its technological expertise. The group has plenty of capacity to make acquisitions, with net debt to EBITDA currently at c 0.4x, compared with a 3.5x limit on its promissory notes. There is also a 21% equity ratio covenant on the promissory notes, compared with the current 31.9% modified equity ratio. A low equity ratio was one of the reasons why the group carried out its €21m capital increase last year.

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