

TXT e-solutions

Focused on accelerated growth

TXT e-solutions reported 15% year-on-year organic revenue growth for Q321, further boosted by contributions from recent acquisitions HSPI (+21%) and TeraTron (+11%). EBITDA increased 49% over the same period with a small increase in margin to 13.4%. While the pandemic has reduced demand for certain products and services, TXT has managed to expand into other areas organically and via acquisition to win new business (eg sustainable transport, defence, fintech). Diversification, combined with early signs of recovery from TXT's civil aviation and financial services customers, positions the company well to grow this year and next.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/19	59.1	7.6	0.46	0.00	20.6	N/A
12/20	68.8	7.1	0.47	0.04	20.0	0.4
12/21e	91.6	10.2	0.62	0.06	15.1	0.6
12/22e	107.5	13.2	0.80	0.08	11.7	0.9

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

Organic revenue growth 15% in Q321

TXT reported revenue growth of 46.5% for Q321 and 39.5% for 9M21. Excluding contributions from TeraTron (acquired in August) and HSPI (acquired October 2020), the group grew 15% on an organic basis in Q321. EBITDA grew 49.0% y-o-y in Q321 and 43.1% in 9M21, with the margin expanding 0.2pp in Q321 to 13.4% and 0.3pp in 9M21 to 13.1%. The company closed Q321 with net cash of €3.5m, after paying €10m to acquire TeraTron.

Two more acquisitions; upgrading estimates

On 29 November the company acquired two Italian consulting businesses: Novigo Consulting and LBA Consulting for a total of €5.2m in cash and €1.1m in equity. Operating in the fintech space, both businesses generate EBITDA margins above 20%. We have revised our forecasts to reflect Q321 results and these acquisitions, factoring in higher gross margins which are only partially offset by higher operating expenses. This results in upgrades to our normalised diluted EPS forecasts of 6.7% in FY21 and 16.0% in FY22. After paying for the two recent acquisitions, we forecast a net debt position of €2.3m at the end of FY21, returning to a net cash position of €4.6m by the end of FY22.

Valuation: Discount to peers

TXT continues to trade at a discount to its peer group on all measures. This is despite the deployment of a large proportion of TXT's cash balance into acquisitions, and revenue growth and profitability above the group average. Evidence of improving demand from civil aviation in the Aerospace & Aviation (A&A) division and the banking sector within the Fintech division, growing revenues from the earlier stage fintech businesses and the successful integration of TeraTron should help to reduce this discount.

Q321 results & acquisitions

Software & comp services

13 December 2021

Price €9.4

Market cap €112m

Net cash (€m) at end Q321 3.5

Shares in issue 11.8m

Free float 50%

Code TXT

Primary exchange Borsa Italiana (STAR)

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (7.5) 3.9 27.0

Rel (local) (4.5) 0.4 3.5

52-week high/low €10.66 €6.76

Business description

TXT e-solutions provides IT, consulting and R&D services to aerospace, aviation, automotive, banking and finance customers.

Next events

FY21 results March 2022

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Review of Q321 results

Exhibit 1: Q321 and 9M21 results highlights

€m	Q321	Q320	y-o-y	9M21	9M20	y-o-y
Revenues	23.0	15.7	46.5%	66.7	47.8	39.5%
Gross profit	10.0	7.5	34.0%	26.6	21.5	23.9%
Gross margin (%)	43.4%	47.5%	-4.1%	39.9%	44.9%	-5.0%
EBITDA	3.1	2.1	49.0%	8.8	6.1	43.1%
EBITDA margin (%)	13.4%	13.2%	0.2%	13.1%	12.8%	0.3%
Normalised EBIT	2.5	1.6	54.9%	7.1	4.7	50.5%
Normalised EBIT margin (%)	10.6%	10.1%	0.6%	10.6%	9.8%	0.8%
Reported EBIT	1.9	1.3	52.0%	5.4	3.4	58.7%
Reported EBIT margin (%)	8.4%	8.1%	0.3%	8.0%	7.1%	1.0%
Reported net income	2.1	0.9	134.7%	4.1	3.6	14.5%
Net cash	3.5	31.9	-89.0%	3.5	31.9	-89.0%

Source: TXT e-solutions

TXT reported 46.5% y-o-y revenue growth in Q321; excluding a €5.0m contribution from acquisitions (HSPI €3.3m, TeraTron €1.7m), organic growth was 15% y-o-y. Gross profit was 34% higher y-o-y and gross margin of 43.4% was 4.1pp lower than in Q320 due to a lower proportion of high-margin software sales in the quarter. EBITDA increased 49% y-o-y resulting in EBITDA margin expansion of 0.2pp to 13.4%. Normalised EBIT margin increased by 0.6pp over the same period to 10.6%. With net finance income of €0.3m and an adjustment to tax to reflect a 28% rate for the nine-month period to the end of September (9M21), reported net income increased 135% y-o-y. Net cash declined from €11.1m at the end of H121 to €3.5m at the end of Q321, reflecting the acquisition of TeraTron for €10.1m offset by operating cash inflow of €2.4m.

Exhibit 2: Divisional performance

€m	Q321	Q320	y-o-y	9M21	9M20	y-o-y
Aerospace & Aviation total revenue	13.8	9.8	40.1%	37.1	30.7	20.9%
Software licenses & maintenance	1.6	1.9	-15.1%	5.2	5.7	-8.3%
Services	12.2	7.9	53.4%	31.9	25.0	27.5%
EBITDA	2.3	1.5	55.8%	5.5	4.3	26.9%
EBITDA margin	16.7%	15.0%	1.7%	14.8%	14.1%	0.7%
Fintech total revenue	9.2	5.9	57.3%	29.6	17.1	73.0%
Software licenses & maintenance	0.5	0.2	128.2%	1.2	0.9	36.1%
Services	8.7	5.6	54.4%	28.5	16.3	75.0%
EBITDA	1.1	0.6	83.0%	3.6	1.8	99.4%
EBITDA margin	12.1%	10.4%	1.7%	12.1%	10.5%	1.6%
Group software licenses & maintenance revenue	2.2	2.1	0.6%	6.4	6.5	-2.5%
Group services revenue	20.9	13.6	53.8%	60.4	41.3	46.2%

Source: TXT e-solutions

A&A division: 'TXT flies again'

A&A saw year-on-year revenue growth of 40% for Q321 and 21% for 9M21. Excluding TeraTron revenue of €1.7m, organic revenue growth was 23% for Q321 and 15% for 9M21. Software revenue is lower this year than last, as demand from the civil aviation sector has been weaker due to the pandemic. Services revenue has grown strongly over the year, and excluding TeraTron, was 33% higher in Q321 and 21% higher for 9M21.

As we have previously written, TXT has seen strong demand from the defence sector which has helped offset weakness in the civil aviation market. The company has completed the integration of TeraTron and is now ready to drive the growth of that business. Management is seeing signs of activity in the civil aviation market and also sees opportunities arising from zero emissions programmes and urban mobility, prompting its statement 'TXT flies again'.

So far in Q4:

- TXT has been selected by the European Space Agency's Space Solutions initiative to undertake a study aimed at the development of a new immersive virtual reality solution for first responder training, using the Pacelab WEAVR platform. The Immersive Search and Rescue project aims to develop remote virtual training for search and rescue professionals, taking advantage of satellite data to create realistic scenarios for dealing with natural disasters.
- In November, TXT won an upfront license for its advanced modelling software from a Chinese institution active in the aviation market.
- A North American airline with more than 200 aircraft and 100 destinations is trialling Pacelab FPO software. The company noted that c 90% of trials typically convert into commercial contracts.
- The company is negotiating with a North American cargo line which has successfully completed a trial.

The company had previously disclosed that PACE will supply licences for its preliminary aircraft and systems design suite and its route and aircraft economic analysis tool to the Aerospace Technology Institute's (ATI) FlyZero Project. The project, led by ATI and backed by the UK government, is investigating the design challenges, manufacturing requirements and market opportunities of zero-carbon emission aircraft. Also in the sustainability area, the company is working with major European e-VTOL (electrical vertical take-off and landing) OEMs and recently joined the #1000 solutions challenge, an initiative by the Solar Impulse Foundation¹.

Fintech division

The Fintech division saw year-on-year revenue growth of 57% for Q321 and 73% for 9M21. HSPI contributed revenue of €3.3m in Q321 and €10.5m in 9M21; excluding this, revenue was flat in Q321 and grew 12% in 9M21 (which benefited from a full nine-months contribution from MAC Solutions, acquired in July 2020). The software testing business, Assioma, has seen weaker demand through the pandemic but management believes it is starting to recover. The inclusion of higher margin HSPI for 9M21 helped drive the EBITDA margin up from 10.5% in 9M20 to 12.1% in 9M20.

So far this quarter, one of TXT's start-up software businesses, Faraday, has signed multi-year contracts with the Italian branch of an international banking institution and a regional public IT company.

Fintech acquisitions

On 29 November, TXT announced that it acquired two Italian consulting businesses within the Fintech division.

- **Novigo Consulting:** founded in 2013 as a spin-off from ING Lease, this Brescia-based business has 240 active customers and 25 specialised consultants, operating across six Italian regions and four European countries. The company develops software and applications for the digitalisation of credit brokerage and sales network management for agents in financial activities. It also implements and manages cloud IT infrastructure for financial markets. TXT is paying €3.5m for the company, split 70/30 cash/TXT treasury shares. There are retention and earnout clauses for the three selling shareholders and managers based on FY24 results, with a maximum earnout of €0.8m in equity. Management expects pro forma FY21 revenue to be c €3m with an EBITDA margin of 23%.

¹ [1000+ Solutions to change the world](#)

- **LBA Consulting:** the company was founded in 2007 and has 20 consultants with advanced ERP and CRM skills and more than 30 active international customers. The company also develops and markets proprietary solutions for digital payments and e-commerce. TXT is paying €2.73m in cash for the company. There is a retention and clawback clause based on FY24 and FY26 results. Management expects pro forma FY21 revenue to be c €2.5m with an EBITDA margin of 30%.

Outlook and changes to forecasts

At Q3 results, management highlighted that for M&A it has access to €38m of short-term net financial resources (ie cash plus trading securities less short-term debt) plus 1.24m treasury shares worth c €13m.

We have revised our forecasts to reflect Q321 results, in particular factoring in slightly higher gross margins which are only partially offset by higher operating expenses. We have also added in the Novigo and LBA acquisitions from 1 December. This results in normalised diluted EPS upgrades of 6.7% in FY21 and 16.0% in FY22. We forecast that the company will move to a net debt position by the end of FY21 and cash generation in FY22 should return the company to a net cash position by the end of the year.

Exhibit 3: Changes to estimates

	FY21e old	FY21e new	change	y-o-y	FY22e old	FY22e new	change	y-o-y
Revenues (€m)	90.9	91.6	0.7%	33.2%	101.7	107.5	5.7%	17.4%
Gross margin	39.4%	40.9%	1.5%	(1.7%)	42.0%	43.2%	1.2%	2.2%
Gross profit	35.8	37.5	4.6%	28.0%	42.7	46.4	8.7%	23.8%
EBITDA (€m)	11.8	12.4	4.9%	44.9%	13.7	15.8	15.0%	27.3%
EBITDA margin	13.0%	13.5%	0.5%	1.1%	13.5%	14.7%	1.2%	1.1%
Normalised EBIT (€m)	9.6	10.1	4.9%	53.9%	11.3	13.2	16.7%	31.3%
Normalised EBIT margin	10.6%	11.0%	0.4%	1.5%	11.1%	12.3%	1.2%	1.3%
Reported operating profit (€m)	7.4	7.8	5.9%	141.4%	9.4	11.3	20.0%	44.7%
Normalised net income (€m)	6.8	7.3	7.0%	33.6%	8.1	9.5	17.7%	30.0%
Reported net income (€m)	5.2	5.7	8.7%	25.2%	6.7	8.1	21.3%	42.8%
Normalised diluted EPS (€)	0.58	0.62	6.7%	32.8%	0.69	0.80	16.0%	28.4%
Reported basic EPS (€)	0.45	0.49	8.4%	24.4%	0.57	0.69	19.6%	41.1%
Net cash/(debt) (€m)	2.4	(2.3)	(197%)	(111%)	9.0	4.6	(48.6%)	(298%)
Dividend (€)	0.06	0.06	0.0%	50.0%	0.08	0.08	0.0%	33.3%

Source: Edison Investment Research

Valuation

The table below shows TXT's valuation versus its peer group of European software and services providers. TXT continues to trade at a discount to its peer group on all measures, despite the deployment of a large proportion of the company's cash balance into acquisitions, and revenue growth and profitability above the group average. We expect this discount to reduce as TXT provides evidence of:

- **A&A:** the resumption/acceleration of orders from customers in COVID-19-hit sectors, particularly civil aviation; successful integration of the TeraTron acquisition.
- **Fintech:** the early-stage businesses (TXT Risk Solutions, TXT Working Capital Solutions) starting to generate material revenues and reaching break-even; banks resuming normal activity for software testing; international revenues growing; successful integration of Novigo and LBA.
- Overall, software revenues growing as a percentage of the total, as these generate much higher gross margins.

Exhibit 4: Peer financial and valuation metrics

Company	Share price	Market cap	Rev growth		EBIT margin		EBITDA margin		EV/Sales		EV/EBIT		P/E		Div yield	
	€	€m	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY	CY	NY
TXT	9.40	112	33.2%	17.4%	11.0%	12.3%	13.5%	14.7%	1.2	1.0	10.7	8.2	15.1	11.7	0.6%	0.9%
<u>European IT services companies</u>																
AKKA Technologies	47.96	1,494	3.3%	5.6%	1.1%	5.8%	8.7%	9.6%	1.3	1.2	118.6	20.5	N/A	27.8	0.0%	0.6%
Alten	152.90	5,248	23.0%	11.3%	9.6%	10.1%	12.2%	12.4%	1.8	1.7	19.2	16.4	26.0	22.8	0.7%	0.7%
AtoS	36.07	3,987	-0.9%	1.3%	4.7%	5.5%	10.8%	11.9%	0.6	0.6	12.4	10.4	8.7	7.2	2.7%	2.6%
Cap Gemini	206.00	34,712	13.9%	8.2%	11.6%	12.1%	15.7%	15.9%	2.2	2.1	19.3	17.1	24.2	21.6	1.0%	1.2%
Devoteam	168.50	1,402	10.1%	7.0%	11.0%	11.1%	12.8%	12.8%	1.6	1.5	14.9	13.7	27.5	25.0	0.7%	0.8%
ESI Group	73.80	439	4.0%	6.2%	6.4%	9.6%	10.6%	13.6%	3.4	3.2	52.2	32.8	87.6	55.0	0.0%	0.0%
Reply	179.20	6,693	18.2%	13.4%	14.1%	14.1%	17.4%	17.1%	4.4	3.9	31.5	27.7	44.6	39.6	0.4%	0.4%
Sopra Steria	158.60	3,252	9.4%	5.3%	7.3%	7.9%	11.3%	11.8%	0.9	0.8	11.9	10.4	14.7	12.4	1.5%	1.7%
Average			10.1%	7.3%	8.2%	9.5%	12.4%	13.1%	2.0	1.9	35.0	18.6	33.3	26.4	0.9%	1.0%
<i>(Discount)/premium to peers</i>									<i>(42%)</i>	<i>(46%)</i>	<i>(69%)</i>	<i>(56%)</i>	<i>(55%)</i>	<i>(56%)</i>	<i>(28%)</i>	<i>(15%)</i>

Source: Edison Investment Research, Refinitiv (13 December)

Exhibit 5: Financial summary

	€'000s	2016	2017	2018	2019	2020	2021e	2022e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		33,060	35,852	39,957	59,091	68,753	91,558	107,514
Cost of sales		(18,954)	(20,224)	(22,289)	(31,825)	(39,469)	(54,087)	(61,116)
Gross profit		14,106	15,628	17,668	27,266	29,284	37,471	46,398
EBITDA		4,260	3,536	4,098	7,004	8,560	12,402	15,788
Operating Profit (before amort and except)		3,954	3,180	2,755	5,408	6,542	10,066	13,212
Amortisation of acquired intangibles		(264)	(439)	(610)	(1,142)	(1,340)	(1,900)	(1,900)
Exceptionals and other income		(557)	0	(300)	(713)	(1,963)	(347)	0
Other income		0	(69)	0	0	0	0	0
Operating Profit		3,133	2,672	1,845	3,553	3,239	7,819	11,312
Net Interest		48	(208)	(1,284)	2,194	562	100	0
Profit Before Tax (norm)		4,002	2,972	1,471	7,602	7,104	10,166	13,212
Profit Before Tax (FRS 3)		3,181	2,464	561	2,315	5,958	7,919	11,312
Tax		(661)	(710)	4	(1,867)	(1,162)	(2,217)	(3,167)
Profit After Tax (norm)		3,170	2,170	1,204	5,473	5,718	7,320	9,513
Profit After Tax (FRS 3)		2,520	1,754	565	448	4,796	5,702	8,145
Ave. Number of Shares Outstanding (m)		11.7	11.7	11.7	11.7	11.7	11.7	11.9
EPS - normalised (€)		0.271	0.186	0.102	0.456	0.470	0.624	0.801
EPS - normalised fully diluted (€)		0.271	0.186	0.102	0.456	0.470	0.624	0.801
EPS - (IFRS) (€)		0.475	5.874	0.048	0.027	0.391	0.486	0.686
Dividend per share (€)		0.30	1.00	0.50	0.00	0.04	0.06	0.08
Gross margin (%)		42.7	43.6	44.2	46.1	42.6	40.9	43.2
EBITDA Margin (%)		12.9	9.9	10.3	11.9	12.5	13.5	14.7
Operating Margin (before GW and except) (%)		12.0	8.9	6.9	9.2	9.5	11.0	12.3
BALANCE SHEET								
Fixed Assets		25,428	8,860	22,942	34,635	47,411	76,815	73,239
Intangible Assets		21,296	7,332	17,751	24,380	37,652	54,126	52,110
Tangible Assets		1,598	793	3,680	7,929	7,460	6,090	4,530
Other		2,534	735	1,511	2,326	2,299	16,599	16,599
Current Assets		37,085	109,426	134,674	127,052	126,036	102,411	109,915
Stocks		3,146	2,528	3,141	4,156	4,749	5,049	5,349
Debtors		26,369	17,215	16,992	24,150	41,193	50,169	58,912
Cash		7,570	89,683	114,541	98,746	80,094	47,193	45,654
Other		0	0	0	0	0	0	0
Current Liabilities		(21,051)	(13,612)	(29,366)	(43,129)	(55,446)	(62,587)	(67,583)
Creditors		(20,243)	(12,937)	(12,062)	(17,823)	(24,811)	(31,952)	(36,948)
Short term borrowings		(808)	(675)	(17,304)	(25,306)	(30,635)	(30,635)	(30,635)
Long Term Liabilities		(7,180)	(4,781)	(41,903)	(36,538)	(32,138)	(23,638)	(15,138)
Long term borrowings		(1,391)	(1,688)	(36,882)	(32,029)	(27,398)	(18,898)	(10,398)
Other long term liabilities		(5,789)	(3,093)	(5,021)	(4,509)	(4,740)	(4,740)	(4,740)
Net Assets		34,282	99,893	86,347	82,020	85,863	93,001	100,433
CASH FLOW								
Operating Cash Flow		10,676	119	2,039	(354)	1,244	9,920	11,741
Net Interest		105	(208)	(69)	3,102	(988)	100	0
Tax		(2,022)	379	(624)	(229)	(1,332)	(2,217)	(3,167)
Capex		(738)	(661)	(548)	(916)	(1,156)	(850)	(900)
Acquisitions/disposals		(5,403)	82,250	1,314	(2,178)	(11,701)	(30,755)	0
Financing		(828)	(6)	(7,208)	(4,287)	(2,648)	(130)	0
Dividends		(2,931)	(3,496)	(11,710)	(5,781)	0	(468)	(713)
Net Cash Flow		(1,141)	78,377	(16,806)	(10,643)	(16,581)	(24,401)	6,961
Opening net debt/(cash)		(8,259)	(5,371)	(87,320)	(60,355)	(41,412)	(22,061)	2,340
HP finance leases initiated		0	0	(2,788)	(2,500)	0	0	0
Other		(1,747)	3,572	(7,371)	(5,800)	(2,770)	0	0
Closing net debt/(cash)		(5,371)	(87,320)	(60,355)	(41,412)	(22,061)	2,340	(4,621)

Source: TXT e-solutions, Edison Investment Research

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