

STEMMER IMAGING

Technology
5 November 2018

Record maiden full year results

STEMMER IMAGING (SI) started its life as a listed company by posting the highest full-year revenues in its history. We expect further improvement as SI benefits from its broad product portfolio, customisation expertise and extensive customer base across many markets to take advantage of double-digit growth in the machine vision industry. This organic growth is being supplemented with acquisitions, as management has allocated half of the €51m (gross) raised at the IPO in February for expansion.

Double-digit growth in revenues and EBITDA

Record group sales of €100.6m in FY18 represented a 14% y-o-y increase. This was faster than the overall market, which management estimates grew by c 11%. €1.7m of the €12.3m increase was attributable to the Data Vision acquisition, the remainder primarily to organic growth in Germany and Benelux. After adjusting for costs associated with the IPO transaction and related one-off bonuses, EBITDA climbed by 46% to €11.1m, while EBITDA margin improved by 2.4pp to 11.0%. This is at the top end of management guidance which was revised upwards in May.

Executing on acquisition strategy

As one of Europe's largest independent providers of machine vision technology, SI has the scale to support a highly technical offer: advising on component selection, providing feasibility studies for customers and tailoring machine vision systems to meet specific customer requirements. All of this drives margin and aids customer retention. SI's scale also enables it to act as a consolidator in the market, in effect creating a virtuous circle. In January, the acquisition of Data Vision in the Netherlands added complementary products, particularly software, and made SI the largest machine vision supplier in the Benelux region. French competitor ELVITEC was acquired in July (signed). In October, SI took a strategic stake in Perception Park, adding hyperspectral imaging software to its product portfolio.

Valuation: High rating for strong revenue growth

SI's prospective EV/EBITDA and P/E multiples are close to the calendarised mean for our sample of companies making machine vision components and systems (eg SI's June 2019 P/E is 28.0x vs 29.4x mean). Since consensus estimates indicate that SI can grow at least as quickly as other companies in this sector (17.3% CAGR in revenues FY18-20 vs 13.3% mean), a similar rating appears justified, even though SI does not achieve as high an EBITDA margin as the others.

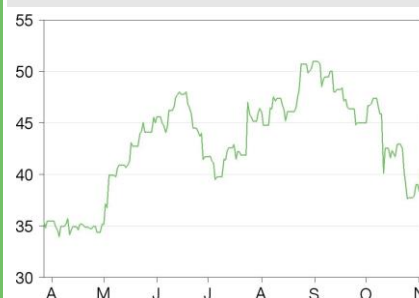
Consensus estimates

Year end	Revenue (€m)	EBIT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
06/17	88.3	5.8	0.67**	0.0	95.8	N/A
06/18	100.6	8.9	1.18**	0.50	91.6	1.2
06/19e	123.0	11.2	1.47	0.50	28.0	1.2
06/20e	139.0	14.9	1.84	0.50	22.4	1.2

Source: Bloomberg. Note: *Adjusted for IPO and other non-recurring items. **On number of shares at listing.

Price €41.2
Market cap €269m

Share price graph



Share details

Code	S9I
Listing	Deutsche Börse Scale
Shares in issue	6.5m
Last reported net cash end June 2018 (including €5.0m short-term securities)	€51.8m

Business description

STEMMER IMAGING Group (SI) is Europe's leading independent provider of machine vision technology solutions to science and industry, selling both directly and indirectly, via system integrators or OEMs.

Bull

- Demand for machine vision solutions growing, driven by increased automation and IoT.
- Broad supplier base combined with in-house development capability enables SI to offer precisely tailored solutions to customers.
- Not dependent on individual industry sectors.

Bear

- Business model difficult to implement in the US.
- Meaningful proportion of market purchases directly from component suppliers.
- Low free-float of 40%

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Financials

Record revenues in FY18

Revenue grew by 14.0% year-on-year to a record €100.6m. This was faster than the overall market, which management estimates grew by around 11%. €1.7m of the €12.3m increase was attributable to the Data Vision acquisition, the remainder primarily to organic growth in Germany and the Benelux region. SI was able to take advantage of a positive market environment in the machine vision industry because of its broad customer base across numerous application areas and industries. Gross margin increased by 1.5pp to 36.4% because of improved purchasing conditions and a rise in the proportion of proprietary, higher-margin products such as software and services from 10.9% of the total to 11.1%. This is in line with management's stated strategy of increasing the proportion of revenues from services. After stripping out bonuses payable in both FY17 and FY18, personnel costs grew by c 6%, reflecting an increase in the number of employees and wage increases. After stripping out €3.2m IPO related costs, other operating expenses grew by c 9%, mainly because of higher marketing costs. After adjusting for costs associated with the IPO transaction and related one-off bonuses, EBIT climbed by 52.7% to €8.9m as EBIT margin improved by 2.2pp to 8.8%. Revenue growth, gross margin and adjusted EBIT were all higher than management's original expectations.

Strong balance sheet

Operating cash flow reduced from €5.2m in FY17 to €3.3m in FY18. Key movements included €5.6m rise in inventories and trade receivables, both of which were linked to higher revenues, and a €2.9m cash payment to employees that was agreed as part of the transfer of ownership prior to the IPO. At €0.9m, capital expenditure was slightly lower than FY17, though as management follows an asset-light model, capital expenditure is typically modest. Net cash, including short-term securities held as a proxy for cash, increased by €46.2m during the period to €51.8m at the end of June 2018. The increase is primarily attributable to the IPO in February, which generated €51.0m (gross). There is no debt on the balance sheet.

Outlook: Market prospects are good

A report published in July 2017 by research specialists MarketsandMarkets forecast that the global industrial robotics market would grow from US\$38.1bn in 2016 to US\$71.7bn by 2023, a CAGR of 9.6%. The machine vision section of the German Mechanical Engineering Industry Association (VDMA) predicts a 7% increase in turnover from the German machine vision industry during 2018 to €2.8bn. Management has not issued formal guidance for FY19 yet. Noting a positive market environment, product development including the new release of the Common Vision Blox software and focused international expansion, management expects revenues to increase compared with FY18, and a slight improvement in both gross margin and EBITDA margin.

Successful IPO

STEMMER IMAGING AG listed on the Scale index of the Deutsche Börse on 27 February 2018. As part of the listing process it raised €51m (gross) through the issue of 1.5m new shares at €34.0/share, a 30% increase in capital. At the same time, as part of the placement, STEMMER IMAGING Holding, which had previously held a 100% stake in STEMMER IMAGING AG, sold 1.5m existing shares (including an over-allotment option), reducing its stake to 54%. The funds raised by the company are being used primarily to finance acquisitions and to invest in product development, particularly software.

Progress on execution of strategy

SI has an exemplary track record of identifying and integrating acquisitions (see our February [initiation note](#)). Management is using the funds raised from the IPO to continue this strategy, selecting companies that will consolidate its position in existing geographies, expand its footprint or add complementary products, particularly software.

Strengthening distribution network

In January 2018, SI acquired Netherlands-based Data Vision, a highly specialised provider of machine vision solutions and components, thus becoming the largest machine vision supplier in the Benelux region as measured by revenue. Management expects that the significant overlap between products offered by Data Vision and SI will provide substantial purchasing synergies. In addition, it is likely that Data Vision will be able to win business with much larger companies now that it is part of a bigger group. This happened with Iris Vision, also in the Netherlands, which SI acquired in 2012. The consideration for Data Vision was €3.3m, payable in cash. We estimate that if Data Vision had been part of the group from the start of FY18, it would have contributed €5.9m revenues and €2.0m gross margin.

The acquisition of French competitor ELVITEC in July (signed) for a provisional purchase price of €5.1m follows a similar rationale. Management estimates that the acquisition will generate annualised revenues of around €9m with an EBIT margin of around 11% during FY19.

Enhancing product portfolio

In October, SI took a strategic stake in Perception Park for a low single-digit million euro sum, thereby adding hyperspectral imaging software technology to its product portfolio. Perception Park's software platform processes complex hyperspectral data at the molecular level, extracting highly precise colour coordinates, chemical material properties and layer thickness information. This information is used in machine vision applications for food-processing, mining, healthcare and recycling, all of which applications have high growth potential. The two companies have been working together since January 2016.

New geographic market penetration

In August, SI announced it had signed a memorandum of understanding with the Chinese provider of machine vision technology Nanjing Inovance, which is a subsidiary of the publicly traded Shenzhen Inovance Technology, a leading manufacturer of automation components in China. This takes SI into one of the most dynamically growing automation markets where demand is high, yet knowledge of how to implement image processing systems is relatively low. Both partners believe that the cooperation will generate significant revenues with above-average growth rates in China. In particular, SI expects high sales potential for its proprietary machine vision software Common Vision Blox China is a key potential market. Statistics from VDMA show that turnover from the German machine vision industry grew by 17% in 2017 to €2.6bn, with domestic sales growing by 8% and exports by 23%. The two most important export markets were China and North America which collectively account for 26% of total revenues. In 2017, exports to China exceeded those to North America for the first time.

Valuation

At the end of the first day of trading, the share price was €37.70, which represented a gain of more than 10% on the issue price of €34.00. The share price peaked at €51.37 on 3 September 2018, but although it has dropped back since then it is still substantially higher than the IPO price.

SI's prospective EV/EBITDA and P/E multiples are close to the calendarised mean for our sample of companies making machine vision components and systems (eg SI's June 2019 P/E is 28.0x vs 29.4x mean). Since consensus estimates indicate that SI can grow at least as quickly as other companies in this sector (17.3% CAGR between FY18 and FY20 vs 13.3% mean), plus it is acting as an industry consolidator, which might command a premium, a similar rating appears justified even though SI's EBITDA margins are lower (11.5% vs 27.7% mean) because it is providing systems that contain a high proportion of third party hardware. While SI is trading at a premium to the value-added distributors (eg June 2019 P/E is 22.4x vs 14.2x mean), none of these are focused on the high growth machine vision industry.

Exhibit 1: Peer comparison (calendarised)

Company	Market cap (€m)	EV/EBITDA June 2019 (x)	EV/EBITDA June 2020 (x)	P/E June 2019 (x)	P/E June 2020 (x)	Year 1 EBITDA margin	CAGR (%)
Manufacturers							
Basler	535	13.8	11.8	25.1	21.6	21.7%	14.3%
Cognex Corp	6,508	23.9	19.1	31.4	24.6	31.5%	12.7%
Isra Vision	822	15.2	13.2	31.6	26.8	30.1%	12.7%
Mean		17.6	14.7	29.4	24.4	27.7%	13.3%
Value-add distributors							
Addtech	1,146	12.4	11.4	15.8	14.5	10.9%	13.1%
APC Technology Group	14	8.7	7.1	9.7	7.5	6.7%	12.8%
Diploma	1,596	14.8	13.9	20.9	19.7	18.3%	7.4%
discoverIE Group	338	9.7	9.2	15.3	14.2	8.3%	6.9%
Electrocomponents	2,976	10.8	9.8	16.4	14.8	13.0%	7.1%
Solid State	31	7.3	-	12.3	-	7.5%	3.9%
Mean		10.6	10.3	15.1	14.2	10.8%	8.5%
STEMMER IMAGING	269	18.4	14.8	28.0	22.4	11.5%	17.3%

Source: Bloomberg. Note: Prices as at 24 October 2018.

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