EDISON

SNP Schneider-Neureither & Partner

Interim results

Attractive business drivers are sustained

Software & comp services

While SAP S/4HANA transformation project deferrals impacted on H1 performance, SNP remains confident that there will be a recovery in H2 and beyond. SAP, the Walldorf-based software giant, has been successfully selling its S/4HANA business suite, but we understand these sales are predominantly for small customers and many large enterprises have been deferring data transformations to S/4HANA. However, SNP remains highly confident that the wave of S/4HANA transformations is building up and believes it is the best-placed participant to deliver on this wave of projects with its sophisticated software-based approach using the CrystalBridge platform. We have cut our forecasts towards the top of the reduced guidance range. While the shares look punchy on c 26x our FY19e earnings, the rating could fall quickly as new projects come through.

Year end	Revenue (€m)	PBT* (€m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/16	80.7	6.4	109.7	39.0	16.5	2.2
12/17	122.3	0.2	(7.4)	0.0	N/A	0.0
12/18e	137.9	(4.1)	(57.3)	0.0	N/A	0.0
12/19e	153.4	5.9	70.4	30.0	25.7	1.7

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

Interim results: H1 organic growth was 2%

H1 revenue grew by 35% to €65.0m, including 2% organic growth, along with €16.0m from acquisitions. The group swung to an EBITDA loss of €1.7m from positive EBITDA of €1.3m in H117 (SNP's methodology). The numbers were below expectations, as outlined in the SNP preliminary results release in late July. Net debt increased by €3.2m over the three months to close at €35.8m at end-June. All regions, except for the US, grew significantly. Due to the low utilisation rates in the US, 25 jobs were eliminated in the US in Q1. While the book-to-bill ratio slipped to 0.79x in Q2, the group headed into H2 with a healthy backlog of €63.3m. The group's alliance with IBM Services to target the SAP S/4HANA transformation market has begun well, with €1m of orders and a €45m pipeline already in place.

Forecasts: FY19 and FY20 revenues come back 7%

We have cut our revenue forecasts by 9% in FY18 and 7% in FY19 and FY20. We forecast the group to generate a small profit in H218, but to be loss-making overall in FY18. Our adjusted EPS forecasts come back by 56% in FY19 and by 34% in FY20. We now forecast the group to end FY18 with net debt of €42.8m (previously €35.9m), which eases to €40.9m at end-FY19 and falls to €34.9m at end-FY20.

Valuation: Strong growth play in the ERP space

The stock trades on c 26x in FY19e falling to c 13x in FY20e. Our discounted cash flow valuation (based on c 7% organic revenue CAGR over 10 years, 10% WACC, 14.8% long-term margin and 2% terminal growth) is €32/share, c 77% above the current share price. Increasing the organic revenue CAGR to 10% increases the valuation to c €44/share, while a 15% CAGR takes the valuation to c €73/share, with other variables remaining constant.

23 August 2018

Price	**€18.10**
Market cap	**€99m**

Net debt (€m) at 30 June 2018	35.8
Shares in issue	5.5m
Free float	53.0
Code	SHF
Primary exchange	Frankfurt (Xetra)
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(21.7)	(48.1)	(47.9)
Rel (local)	(20.6)	(44.9)	(48.6)
52-week high/low		€37.40	€16.4

Business description

SNP Schneider-Neureither & Partner is a software and consulting business focused on supporting customers in implementing change, and rapidly and economically tailoring IT landscapes to new situations. It has developed a proprietary software suite, CrystalBridge and Transformation Backbone with SAP LT (T-B), which automatically analyses and applies and tracks changes in IT systems

Next events

Q3 results	30 October 2018
German Equity Forum	26-28 November 2018

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Interim results: 2% organic growth in both Q1 and Q2

H1 revenue grew by 35% to €65.0m, including 2% organic growth, along with €16.0m from the acquisitions of Innoplexia, SNP Poland and Adepcon. The group swung to an EBITDA loss of €1.7m from positive EBITDA of €1.3m in H117 (SNP's methodology). On our methodology calculations, these numbers were a €2.1m loss and a €1.2m profit respectively. The loss was due to a poor performance in the US, and included €1.8m of restructuring expenses, while the DACH region generated moderate profits and other areas delivered normal levels of profitability.

These numbers were below the expectations affirmed at the time of the Q1 results in late April, and in late July SNP issued preliminary results and cut its FY18 revenue guidance to €135-140m from €150-155m, with a slightly negative EBIT margin (previous guidance was mid-single digits). The EBIT margin in H2 is expected to be "positive, single digit" while FY18 EBITDA is expected to be in the lower to mid-single digit millions of euros. SNP is very confident that there will be a rebound in proprietary software sales in H2 and has implemented a price increase. Management remains committed to its "over-riding medium-term target for structural profitability growth".

The primary reason for the expectations miss was the deferral of many S/4HANA projects, as a result of lengthening planning and proof-of-concept (POC) phases. This resulted in lower capacity utilisation for Professional Services, which was exacerbated by heavy recruitment in late 2017, along with reduced proprietary software licence revenue. H1 utilisation rates were c 73-74% against a normal level of c 80%. Revenues from the M&A-driven side (eg mergers, carve-outs) also disappointed, which we believe reflects the lumpiness of deals as well as the senior-level changes in the sales team. Additionally, the company said that pipeline conversion rates have been lower than normal at c 40%, from 50%, which was due to the current high level of market engagement.

Exhibit 1: Quarterly analysis

€000s	FY16	Q117	Q217	Q317	Q417	FY17	Q118	Q218	Q3-Q418	FY18e	FY19e
Professional services	66,640	19,089	22,151	25,936	31,157	98,333	25,441	26,867	52,543	104,851	117,267
Cloud							424	565	1,011	2,000	2,190
Licences	11,982	1,733	3,042	5,935	8,389	19,099	3,697	3,888	15,219	22,804	24,971
Maintenance	2,063	776	1,237	1,140	1,758	4,911	1,991	2,172	4,076	8,239	9,022
Total revenue	80,685	21,598	26,430	33,011	41,304	122,343	31,553	33,492	72,850	137,895	153,449
Other operating income*	1,228	235	295	171	1,217	1,918	833	1,015			
Cost of materials	(8,276)	(2,260)	(3,244)	(7,037)	(6,674)	(19,215)	(5,135)	(5,346)			
Personnel costs	(47,207)	(14,657)	(15,511)	(18,849)	(22,455)	(71,472)	(21,363)	(23,010)			
Other operating expenses	(17,811)	(6,692)	(6,461)	(7,156)	(9,626)	(29,935)	(7,183)	(7,875)			
Impairments on receivables etc								(225)			
Other taxes	(95)	(28)	(277)	(32)	(196)	(533)	(118)	(137)			
Op costs (before depreciation)	(72,161)	(23,402)	(25,198)	(32,903)	(37,572)	(119,075)	(32,966)	(35,578)	(68,658)	(137,202)	(141,960)
Adjusted EBITDA	8,524	(1,804)	1,232	108	3,732	3,268	(1,413)	(2,086)	4,191	692	11,489
Depreciation*	(1,010)	(344)	(390)	(493)	(528)	(1,755)	(808)	(936)	(1,744)	(3,488)	(4,274)
Adjusted operating profit	7,514	(2,148)	842	(385)	3,204	1,513	(2,221)	(3,022)	2,447	(2,796)	7,215
Operating Margin	9.3%	(9.9%)	3.2%	(1.2%)	7.8%	1.2%	(7.0%)	(9.0%)	3.4%	(2.0%)	4.7%
Net interest	(1,137)	(577)	(181)	(218)	(351)	(1,327)	(287)	(351)	(662)	(1,300)	(1,300)
Edison profit before tax (norm)	6,377	(2,725)	661	(603)	2,853	186	(2,508)	(3,373)	1,785	(4,096)	5,915
Amortisation of acq'd intangs*	(657)	(250)	(300)	(350)	(1,121)	(2,021)	(400)	(400)	(800)	(1,600)	(1,600)
Associates	8	0	(1)	12	(35)	(24)	0	0	0	0	0
Earnings before tax	5,728	(2,975)	360	(941)	1,697	(1,859)	(2,908)	(3,773)	985	(5,696)	4,315
New orders and backlog											
Incoming orders	95,600	24,400	33,200	37,400	35,700	130,700	40,900	26,300			
Quarterly revenues	80,685	21,598	26,430	33,011	41,304	122,343	31,553	33,492			
Book-to-bill ratio	1.18	1.13	1.26	1.13	0.86	1.07	1.30	0.79			
Backlog		40,800	48,500	62,200	61,300		70,200	63,300			

Source: Company accounts, Edison Investment Research. Note: *Quarterly amortisation of acquired intangibles is estimated data.

The S/4HANA project deferrals related to the complexity of SAP S/4HANA and clients choosing to wait for a greater "maturity level" of S/4HANA before planning a full transition. In light of feedback from its customers, SNP is confident that this is now happening and many customers are close to proceeding. SNP estimates that there are c 50,000 enterprises that need to transition to S/4HANA and believes that a tsunami of transformations is building up.

SAP S/4HANA was launched in 2015, and while SAP has had great success with its new fourth-generation Enterprise Resource Planning (ERP) suite, with more than 8,900 customers, up 41% over the year. Nevertheless, we understand that most of these are small customers that are not in SNP's targeted market. SNP has not yet booked, nor is it aware of any competing large-scale S/4HANA transformations. However, some of SNP's largest customers are looking to transition to S/4HANA using SNP's T-B software and SNP says it is currently engaged in more than 20 SAP S/4HANA POCs that relate to large enterprise customers. Consequently, SNP expects the average deal size to rise significantly over the next 12 months. SNP says the number of POCs has been growing strongly. It estimates that a typical large-scale transformation to SAP S/4HANA would take around five years to implement, and believes it can reduce the project duration to around two to three years through using its highly automated Bluefield template-based approach.

Measures have been taken to improve the efficiency of the business, including cost reductions, working capital improvements and targeting customers at a higher management level. A key goal is to improve the value proposition and, in wake of the landmark $6m Hewlett-Packard carve-out, seek to take a higher share of M&A project costs. At the lower end, SNP is working on a strategy to target SMEs using a partner model. The US business had not been meeting expectations and hence 25 jobs were eliminated in Q1, leaving c 75 jobs in the US. The group had 1,350 employees at end-June, up from 1,341 at year end, but down from 1,363 as at end March. Further headcount reductions are not anticipated, as skilled employees are hard to recruit, and the company highlights that it has a revenue problem rather than a cost problem.

All regions, except for the US, grew significantly. The share of revenues from DACH (Germany Austria and Switzerland) countries slipped from 61% to 50%, with the increase predominantly due to the acquisitions in Poland and South America. The UK grew revenues by 20%, while Asia was flat, and the US fell by 8%. The South American business, which was acquired in mid-2017, is in good health, and this business is now being adapted to sell SNP's proprietary software and transformation consultancy. China and South-East Asia are growing. However, SNP is cautious about selling its software in Asia due to potential piracy reasons, and it highlights the primary focus regions as Germany, the UK, US and Switzerland.

Software sales grew by 31% organically, while professional services declined by 6% on this basis. Software sales included €4.2m of low-margin software resales (€0.5m in H117). Licence sales grew by 59% to €7.6m, but excluding resales, SNP's proprietary software licence sales fell by 21% to €3.4m. Also included in the software category was €1.0 of cloud services, which came to SNP with the BCC acquisition, and maintenance revenues, which more than doubled to €4.2m. The S/4HANA project delays were reflected in the 6% organic decline in professional services and the 21% decline in the proprietary software sales. Transformation Backbone revenues rose by 32%, including maintenance revenues, while Data Provisioning & Masking jumped by 54% and Interface Scanner rose by 13%.

Management is bullish on its global alliance with IBM Services, which is targeting the SAP S/4HANA transformation market. The alliance is targeting IBM's huge customer base and SNP emphasises that due to the huge number of S/4HANA projects, these can only be achieved using an automated approach. SNP has already trained the IBM Services sales team on the SNP Bluefield approach and it says the pipeline is growing by the week. SNP has already received c €1m of orders and a €45m pipeline is in place (of which half is licences and half consultancy).

Initially, SNP will be handing the services work, but over time it will train IBM's staff while booking the software revenue.

Management changes

Henry Göttler, head of Asian operations, left the business in April. David Kenneson resigned from his position as chief revenue officer in July after joining in January. The group is switching back to an MD model and is seeking a CEO in the US and a chief operating officer for the group. Dr Uwe Schwellbach was appointed chief financial officer in July. Dr Schwellbach is responsible for finance and HR.

Cash flow and balance sheet

The group continues to maintain healthy cash balances following its capital-raising last year. SNP recently amended the presentation of its accounts, with financial liabilities now including acquisition liabilities (see our previous update note). The H1 operating cash outflow was €5.3m (implying a €0.6m outflow in Q2) and, after net capex of €2.0m, the free cash outflow was €7.1m. The group paid €7.0m in acquisition payments during the half. Group's net debt increased by €3.2m over the quarter to €35.8m. There is also a small pension deficit that we have included in our DCF valuation.

Exhibit 2: Financial position

€m	31-Dec-17	31-Mar-18	30-Jun-18
Cash	(33.9)	(24.3)	(18.5)
Current financial liabilities	11.2	7.4	6.3
Non-current financial liabilities	49.5	49.5	48.0
Net debt/(cash)	26.8	32.6	35.8
Pension deficit	1.5	1.6	1.6
Adjusted net debt/(cash)	28.4	34.2	37.4

Source: Company accounts

Forecasts: FY19 and FY20 revenues come back 7%

We have cut our revenue forecasts by 9% in FY18 to €137.9m and 7% in FY19 and FY20 to €153.4m and €166.6m respectively. We forecast the group to generate a small profit in H218, mainly due to a strong rebound in proprietary software sales and benefits from the restructuring programme, but to be loss-making overall in FY18. Given the growing number of S/4HANA POCs, we would expect revenues from these projects to start flowing from FY19. Our adjusted EPS forecasts come back by 56% in FY19 and by 34% in FY20. Our dividend forecasts shift back by one year and we now forecast no dividend in FY18 (previously 30c), 30c in FY19 (40c) and 40c in FY20 (50c). We now forecast the group to end FY18 with net debt of €42.8m (previously €35.9m), which eases to €40.9m (€30.8m) at end-FY19 and falls to €34.9m (€21.5m) at end-FY20.

Exhibit 3: Forecast changes

	2018e			2019e			2020e		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Revenue									
Professional services	114,957	104,851	(8.8)	125,556	117,267	(6.6)	136,149	127,158	(6.6)
Cloud	1,800	2,000	11.1	1,971	2,190	11.1	2,149	2,388	11.1
Software licences	27,671	22,804	(17.6)	30,300	24,971	(17.6)	33,035	27,224	(17.6)
Software maintenance	6,821	8,239	20.8	7,469	9,022	20.8	8,143	9,836	20.8
Total software	34,492	31,043	(10.0)	37,769	33,992	(10.0)	41,178	37,060	(10.0)
Group revenue	151,249	137,895	(8.8)	165,297	153,449	(7.2)	179,476	166,606	(7.2)
Growth (%)	23.6	12.7		9.3	11.3		8.6	8.6	
Professional services contribution	5,748	0	(100.0)	8,387	4,691	(44.1)	10,157	8,265	(18.6)
Cloud contribution	90	100	11.1	132	146	11.1	160	178	11.1
Software contribution	7,556	3,104	(58.9)	11,536	8,498	(26.3)	13,607	10,192	(25.1)
Non-segment-related expenses	(6,000)	(6,000)	0.0	(6,120)	(6,120)	0.0	(6,242)	(6,242)	0.0
Operating expenses	(143,855)	(140,690)	(2.2)	(151,362)	(146,234)	(3.4)	(161,794)	(154,214)	(4.7)
Capitalisation of dev costs (net)	(32)	(32)	0.0	(32)	(32)	0.0	(32)	(32)	0.0
Adjusted operating profit (EBIT)	7,394	(2,796)	(137.8)	13,935	7,215	(48.2)	17,682	12,393	(29.9)
Operating profit margin (%)	4.9	(2.0)		8.4	4.7		9.9	7.4	
Growth (%)	(1,555.1)	(284.8)		88.5	(358.1)		26.9	71.8	
Net interest	(1,200)	(1,300)	8.3	(1,000)	(1,300)	30.0	(800)	(1,100)	37.5
Profit before tax norm	6,194	(4,096)	(166.1)	12,935	5,915	(54.3)	16,882	11,293	(33.1)
Amortisation of acquired intangibles	(1,600)	(1,600)	0.0	(1,600)	(1,600)	0.0	(1,600)	(1,600)	0.0
Profit before tax	4,594	(5,696)	(224.0)	11,335	4,315	(61.9)	15,282	9,693	(36.6)
Taxation	(1,858)	1,229	(166.1)	(3,880)	(1,775)	(54.3)	(5,065)	(3,388)	(33.1)
Non-controlling interests	(267)	(267)	0.0	(289)	(289)	0.0	(312)	(312)	0.0
FRS 3 net income	2,469	(4,734)	(291.8)	7,166	2,252	(68.6)	9,906	5,993	(39.5)
Adjusted EPS (c)	74.3	(57.3)	(177.0)	160.1	70.4	(56.1)	210.2	138.7	(34.0)
P/E - Adjusted EPS		N/A			25.7			13.0	

Source: Edison Investment Research

Exhibit 4: Financial summary

€'000s	2015	2016	2017	2018e	2019e	2020e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	56,236	80,685	122,343	137,895	153,449	166,606
Cost of sales	0	0	0	0	0	0
Gross Profit	56,236	80,685	122,343	137,895	153,449	166,606
EBITDA	5,484	8,524	3,268	692	11,489	16,923
Adjusted Operating Profit*	4,222	7,514	1,513	(2,796)	7,215	12,393
Amortisation of acquired intangibles	0	(657)	(2,021)	(1,600)	(1,600)	(1,600)
Exceptionals	356	0	0	0	0	0
Associates	(3)	8	(24)	0	0	0
Operating Profit	4,575	6,865	(532)	(4,396)	5,615	10,793
Net Interest	(828)	(1,137)	(1,327)	(1,300)	(1,300)	(1,100)
Profit Before Tax (norm)	3,394	6,377	186	(4,096)	5,915	11,293
Profit Before Tax (FRS 3)	3,747	5,728	(1,859)	(5,696)	4,315	9,693
Tax	(1,195)	(1,517)	(807)	1,229	(1,775)	(3,388)
Profit After Tax (norm)	2,198	4,860	(620)	(2,867)	4,141	7,905
Profit After Tax (FRS 3)	2,552	4,211	(2,666)	(4,467)	2,541	6,305
Minority interest	0	(147)	234	(267)	(289)	(312)
Adjustments for normalised earnings	0	0	0	0	0	0
Net income (norm)	2,198	4,713	(386)	(3,134)	3,852	7,593
Net income (FRS 3)	2,552	4,064	(2,431)	(4,734)	2,252	5,993
Average Number of Shares Outstanding (m)	3.7	4.3	5.2	5.5	5.5	5.5
EPS - normalised (c)	58.8	109.7	(7.4)	(57.3)	70.4	138.7
EPS - normalised & fully diluted (c)	58.8	109.7	(7.4)	(57.3)	70.4	138.7
EPS - FRS 3 (c)	68.3	94.6	(46.8)	(86.5)	41.1	109.5
Dividend per share (c)	34.00	39.00	0.00	0.00	30.00	40.00
Gross Margin (%)	100.0	100.0	100.0	100.0	100.0	100.0
EBITDA Margin (%)	9.8	10.6	2.7	0.5	7.5	10.2
Adjusted Operating Margin (%)	7.5	9.3	1.2	(2.0)	4.7	7.4
BALANCE SHEET						
Fixed Assets	15,243	30,109	75,171	74,188	72,501	70,504
Intangible Assets	11,675	24,179	67,012	65,380	63,748	62,115
Tangible Assets	1,999	3,161	5,187	5,836	5,782	5,417
Other	1,570	2,769	2,972	2,972	2,972	2,972
Current Assets	29,996	58,424	78,614	58,271	60,182	65,506
Stocks	0	371	371	418	466	506
Debtors	16,084	25,652	43,781	44,346	49,348	53,579
Cash	13,769	31,914	33,877	12,921	9,783	10,836
Current Liabilities	(13,703)	(32,631)	(40,531)	(40,517)	(44,862)	(48,353)
Creditors	(11,101)	(14,523)	(29,295)	(29,281)	(33,626)	(37,117)
Short term borrowings	(2,602)	(18,108)	(11,236)	(11,236)	(11,236)	(11,236)
Long Term Liabilities	(15,513)	(7,327)	(53,157)	(45,583)	(40,583)	(35,583)
Long term borrowings	(12,344)	(5,531)	(49,487)	(44,487)	(39,487)	(34,487)
Other long term liabilities	(3,169)	(1,796)	(3,670)	(1,096)	(1,096)	(1,096)
Net Assets	16,024	48,575	60,097	46,358	47,238	52,074
CASH FLOW						
Operating Cash Flow	1,879	1,005	(5,316)	35	10,754	16,122
Net Interest	(167)	53	(798)	(1,300)	(1,300)	(1,100)
Tax	(554)	(412)	(1,366)	1,147	(1,656)	(3,162)
Capex	(1,779)	(3,451)	(5,234)	(4,137)	(4,220)	(4,165)
Acquisitions/disposals**	(3,228)	(5,923)	(28,783)	(11,701)	(1,716)	0
Shares issued	0	30,129	18,293	0	0	0
Dividends	(483)	(1,264)	(1,932)	0	0	(1,642)
Net Cash Flow	(4,332)	20,137	(25,136)	(15,956)	1,862	6,053
Opening net debt/(cash)	(3,431)	1,176	(8,275)	26,847	42,802	40,940
Other	(275)	(10,686)	(9,985)	0	0	()
Closing net debt/(cash)	1,176	(8,275)	26,847	42,802	40,940	34,888

Source: Source: Company accounts, Edison Investment Research. Note: *Includes exceptional costs in FY17 and FY18. **Includes additional payments for Adepcon in FY18 and FY19, and final payments for RSP, Astrums/Hartung and Harlex in FY18.

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