MAINFIRST
A Stifel Company

Prodware

Software

SPONSORED RESEARCH

20 October 2020

INITIATION OF COVERAGE

Buy

PT: €10.00

Changes	2020E	2021E
Revenue	-	-
EPS	-	-

Key data

Ticker	**ALPRO FP**
Price (19 October 2020)	**€5.52**
Upside to Price Target (%)	81.2
Market Cap (m)	43
Free Float (%)	51.3
Daily Value Traded (m)	0.1
Next Reporting Date	Feb 17 2021
No. of Shares (m)	7.75
1mth perf (%)	(6.5)
3mth perf (%)	(9.2)
12mth perf (%)	(10.7)
12mth high-low (€)	8 - 4

Key financials

(In EUR M)

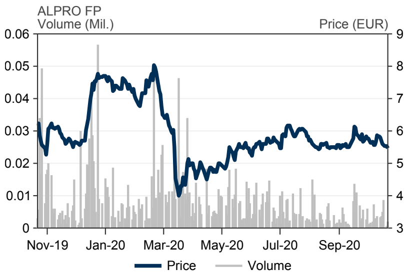
Year to Dec	2019A	2020E	2021E
Group revenue	188	181	186
EBITDA (rep.)	46.5	46.0	46.5
EBIT (rep.)	17.29	18.23	19
EPS (adj.) (c)	1.41	1.67	1.74
DPS (c)	0.04	0.03	0.04
Net debt/(cash)	112.8	119.4	116.9
ROCE (NOPAT) (%)	7.1	7.7	7.9
EPS (adj.) y/y (%)	18.6	17.8	4.7
Net debt/EBITDA	2.33	2.50	2.42
EV/Sales	0.9	0.9	0.9
EV/EBITDA (adj.)	3.3	3.5	3.4
EV/EBIT (adj.)	9.3	9.2	8.6
P/E (adj.)	3.90	3.31	3.17
Dividend yield (%)	0.7	0.6	0.8
Free CF yield (%)	(7.8)	(15.1)	6.6
EV/CE	0.7	0.7	0.7

Prices are as of close 19 October 2020

Completed: 20 October 2020 12:07EDT
Disseminated: 20 October 2020 12:07EDT

All sources unless otherwise stated: Company data, FactSet, MainFirst estimates

Share price performance (indexed)



Initiation of coverage: A key partner in digital transformation

Summary

- **We initiate coverage on Prodware with a Buy rating and price target of €10.00.**
- **Prodware offers a unique end-to-end value proposition to its clients throughout their digital transformation, a trend that has become more apparent during the COVID-19 crisis.**
- **The margin expansion linked to the shift to SaaS and phasing out of ERP related capex is set to propel FCF into positive territory.**
- **We see significant rerating potential as the above trends materialise.**

Key Points

Our investment case for Prodware is based on three key pillars:

Digital transformation should help bolster growth

The group offers a compelling value proposition to its clients and is able to accompany them from end-to-end and internationally, throughout their digital transformation. We consider its focused sector expertise, diversified client base, long track record with a strong management team, and partnerships with leading software houses as supportive characteristics of the business model. We note that the current pandemic has accelerated demand for digital transformation and should boost Prodware's organic growth to 4% in 2022E from 0.3% in 2019 driven by SaaS (+35% CAGR 20-22E).

Shift to SaaS set to lift margins by 150bps over three years

The shift to SaaS-based sales has been brewing for a number of years, but we see the indirect implications of COVID-19 on corporate operations, investment priorities, and remote working, as accelerating this trend. In addition to being a source of recurring revenue, the ramp-up of SaaS (from 21% in 2019 to 50% in 2022) should contribute to a reduced cost structure and therefore increase Prodware's profitability by an estimated 150bps.

End of ERP investments should add over €10m to FCF by 2023

In addition to an improving operating margin, capex will also gradually improve from here as ERP investments (around €10m in 2019) are gradually phased out by 2021. This should propel FCF into positive territory from 2021 and help alleviate concerns around its high level of net debt (2.3x EBITDA end 2019), which has been a prime concern for investors.

Clear operational triggers should support a rerating: we initiate with a Buy rating and €10.00 price target

High capex, increasing indebtedness in recent years, and a slower than expected conversion of the model towards SaaS have weighed on the stock historically. As indicated above, we believe those issues will be addressed in the coming months which should lead to a rerating. Nevertheless, we acknowledge that investors will want to see actual progress before agreeing to pay a full price for the shares, and hence we apply a 20% discount to our valuation methods to reflect these issues, which we may reassess depending on the group's progress. We therefore initiate coverage on Prodware with a Buy rating and price target of €10.00 (DCF and peer-group based).

Caroline David-Tracaz | +33 (1) 7098 3963 | caroline.david-tracaz@mainfirst.com

KEY FINANCIALS AND RATIOS

YEAR TO DECEMBER (IN EUR m)	2019A	2020E	2021E	2022E
PROFIT & LOSS ACCOUNT				
Group revenue	**188**	**181**	**186**	**193**
EBITDA (rep.)	**46.5**	**46.0**	**46.5**	**47.2**
EBIT (rep.)	**17.29**	**18.23**	**19**	**20.3**
Pre-tax results	10.9	12.9	14.0	15.0
Income tax and other items	(0)	(1)	(1)	(2)
Net result group	10.4	12.3	12.8	13.2
Minorities and other items	0.11	0.10	0.10	0.10
Net result shareholders, rep.	**10.5**	**12.4**	**12.9**	**13.3**
EPS, fully diluted (c)	**1.01**	**1.19**	**1.24**	**1.27**
Exceptionals in EBIT	0.01	0	0	0
Profit and Loss Account (adj)				
EBITDA	**48.3**	**47.8**	**48.3**	**49.0**
EBIT	**17.28**	**18.23**	**19**	**20.3**
Operating result (company definition)	17.3	18.2	19.2	20.3
Net result, shareholders	10.5	12.2	12.7	13.1
EPS (adj.) (c)	**1.41**	**1.67**	**1.74**	**1.79**
CASH FLOW STATEMENT				
EBITDA (rep.)	46.5	46.0	46.5	47.2
Cash interest and tax payments	5.74	4.38	4.81	5.48
Change in working capital	3.27	(2)	(0)	(0)
Other operating cash flow items	(22)	(21)	(21)	(22)
Cash flow before capex	**33.7**	**27.1**	**29.8**	**30.3**
Capital expenditure	(37)	(34)	(27)	(22)
Free cash flow	**(3)**	**(6)**	**2.81**	**8.31**
Acquisitions/Disposals/Financial assets	0.11	0	0	0
Dividends, minority payouts	(0)	(0)	(0)	(0)
Equity measures, other	(33)	0.02	0.02	0.02
Change in net cash	(36)	(7)	2.51	7.93
Net cash (debt)	**(113)**	**(119)**	**(117)**	**(109)**
BALANCE SHEET				
Fixed assets	214	214	214	214
Goodwill	34.6	34.6	34.6	34.6
Current Assets	146	138	142	152
t/o Inventories	0.06	0.06	0.06	0.06
t/o Trade receivables	53.2	52.2	53.5	55.6
t/a Cash and equivalents	3.81	(3)	(0)	7.58
Group equity	145	159	173	186
t/o Shareholders equity	144	158	172	186
Interest-bearing liabilities	117	117	117	117
Other liabilties and provisions	98.4	76.4	66.8	63.4
t/ Pension provisions	5.70	5.70	5.70	5.70
t/o Trade libabilities	23.6	27.7	24.0	21.1
Balance sheet total	**360**	**352**	**356**	**366**
Net Working Capital	29.7	24.5	29.5	34.5
Capital Employed (incl. Goodwill)	243	238	243	249
RATIOS				
Revenue y/y (%)	6.7	(3.3)	2.5	4.0
EBITDA Margin (adj.) (%)	25.8	26.4	26.0	25.3
EBIT adj margin (%)	9.2	10.1	10.3	10.5
EPS (adj.) y/y (%)	18.6	17.8	4.7	2.7
Working capital intensity (%)	15.8	13.5	15.9	17.9
DSOs	104	105	105	105
Inventory turnover (Days)	0.11	0.12	0.12	0.11
Net debt (cash) / EBITDA (adj.)	2.33	2.50	2.42	2.22
EBITDA (adj.) / Capex	1.30	1.42	1.79	2.23
Free CF yield (%)	(7.8)	(15.1)	6.6	19.4
Oper. FCF Yield (%)	(5.6)	(6.5)	(1.2)	1.8

Company Snapshot

Investment case summary

Prodware is well placed to capitalise on the growth in the digital transformation market, which has been heightened by the pandemic, with a solid foundation of strategic partnerships and its know-how in terms of innovation. The group offers a unique value proposition that has required investment and reorganisation, to accompany its clients from end to end, throughout their digital transformation. We are confident in Prodware's ability to deliver organic growth of 2.5% in 2021 and 4% in 2022.

In addition to being a source of recurring revenue, the ramp-up of SaaS (from 21% in 2019 to 50% in 2022) should contribute to a reduced cost structure and therefore increase Prodware's profitability to 10.5% from 9.2% in 2019.

Capex will also gradually improve from here as ERP investments are gradually phased out by 2021. This should propel FCF into positive territory from 2021 and help alleviate concerns around its high level of net debt.

Target price methodology

We value Prodware using a mixture of a DCF approach – applying a WACC of 8.7% and a perpetual growth rate of 1.5% – and peer group multiples (EV/Revenue, EV/EBIT, P/E).

High capex, increasing indebtedness in recent years, and a slower than expected conversion of the model towards SaaS have weighed on the stock historically. As indicated above, we believe those issues will be addressed in the coming months which should lead to a rerating. Nevertheless, we acknowledge that investors will want to see actual progress before agreeing to pay full price for the shares, and hence we apply a 20% discount to our valuation methods to reflect these issues, which we may reassess this depending on the group's progress.

Risk to our valuation and rating

- Lack of visibility due to the coronavirus pandemic (cancellation or postponement of projects)
- More competitive pressure, especially in attracting the best employees
- Limited financial manoeuvres in the current economic context

Key dates

- FY-20 Sales release: 17 February 2021

Company description

Founded in 1989, Prodware is a leading French consulting, publishing and IT integration services company. Present in 13 countries worldwide, the company supports SMEs and subsidiaries of major groups through their digital transformation. The group has streamlined its services, focusing on what it masters best, only addressing the Distribution, Manufacturing, Professional services and Retail sectors. What sets Prodware apart is that it has the ability to accompany its customers from end to end with its four key fundamentals: Consulting, Publishing, Implementation and Management services. Prodware has also placed innovation at the heart of its strategy, enabling the group to offer tailor-made solutions with higher added value.

Key products, clients and end markets

Prodware addresses the global digital transformation market which was valued at US$284.4 billion in 2019 and is expected to reach US$1.17 trillion by 2027, at a CAGR of 22.5% over the forecast period 2020-2027. The group, a hybrid of a digital service company and software publisher, is the only French group to be part of Microsoft's "Inner Circle", allowing Prodware to obtain valuable certifications such as Scorefact. Relying on its strategic partnerships and on its know-how in terms of innovation, the group develops its own software bricks to offer adapted and customised solutions. Prodware has strengthened its regional and international footprint in recent years, to offer a responsive local service to over 19,000 clients. International activities represented 60% of sales in 2019 compared with 49% in 2013.

Key shareholders

- Management: 39.1%
- Private investors: 3.3%
- Employees: 1.0%
- Treasury shares: 5.3%

Senior management

- Chairman: Philippe Bouaziz
- CEO: Alain Conrard
- CFO: Stephane Conrard

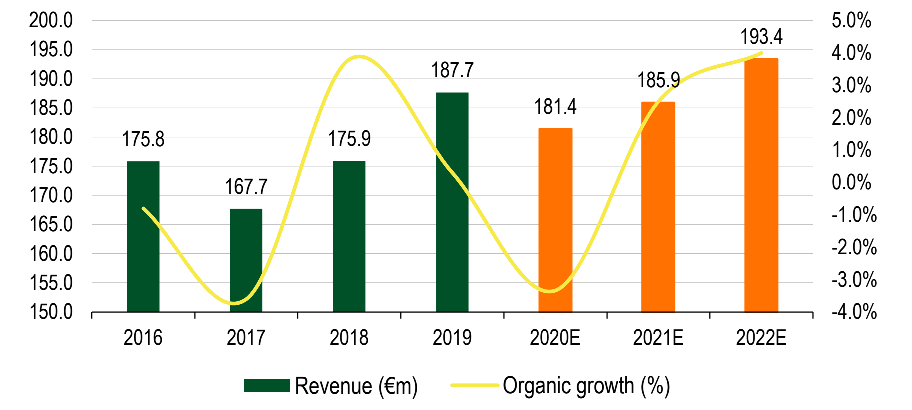
Executive summary

Prodware is specialised in integration, publishing and hosting industry and business line IT solutions. Capitalising on more than 30 years of experience, its strategic partnerships, and its know-how in terms of innovation, the group offers a compelling value proposition to its clients and is able to accompany them from end to end, throughout their digital transformation. Based on the blended average of a DCF and peer group based valuations, we initiate coverage with a Buy rating and price target of €10.00, representing c.80% potential upside from current share price levels. Our investment case for Prodware is based around three key pillars: acceleration of growth driven by digital transformation, higher margins as company shifts to a SaaS model, and FCF acceleration due to falling capex.

Digital transformation should help bolster growth

Prodware provides investors with direct exposure to the attractive structural driver of digital transformation at small and mid-capitalisation companies. Prodware works mostly with French companies and helps them achieve internal expansion. We see its focused sector expertise, diversified client base (of over 19k customers, Top 10 clients around 10% of revenue), long track record with a strong management team, and partnerships with leading software houses as supportive characteristics of the business model. After the exceptional nature of the year 2020, we are confident in Prodware's ability to deliver organic growth of 2.5% in 2021 and 4% in 2022. This is despite the difficulties associated with the transition from the legacy licence into the SaaS-based system (see Figure 2). Relying on both its strategic partnerships which provide access to leading established technologies, as well as using its know-how in terms of innovation, Prodware develops its own software to offer adapted and customised solutions. This has helped the company to establish itself as a strategic partner for its clients.

Figure 1: Revenue forecasts, 2016-22E

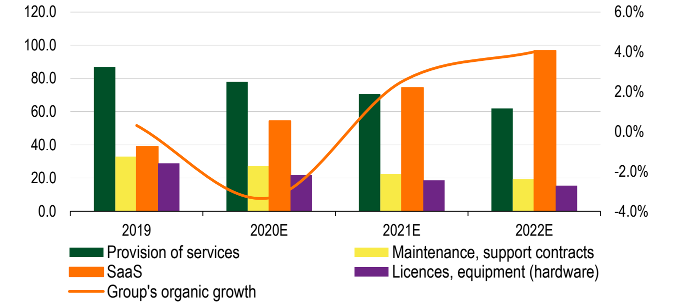


Source: Company data, MainFirst estimates

Shift to SaaS expected to drive margins higher

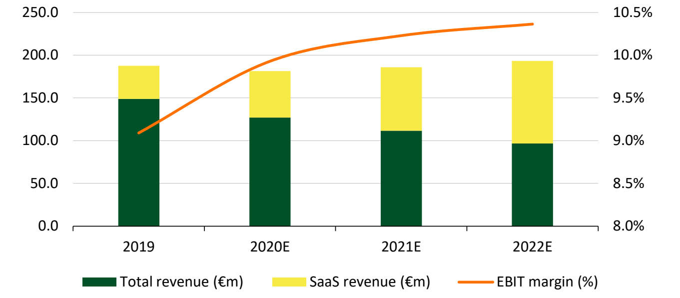
The shift to SaaS-based sales has been ongoing for a number of years, but we see the indirect implications of COVID-19 on corporate operations, investment priorities, and remote working, as accelerating this trend. We conservatively model a 150bps increase in EBIT margins between 2019-22E as the proportion of SaaS revenues increases from 30% to 50%.

Figure 2: Revenue breakdown (€m) and organic growth (%)



Source: Company data, MainFirst estimates

Figure 3: Increasing importance of SaaS revenues (€m)



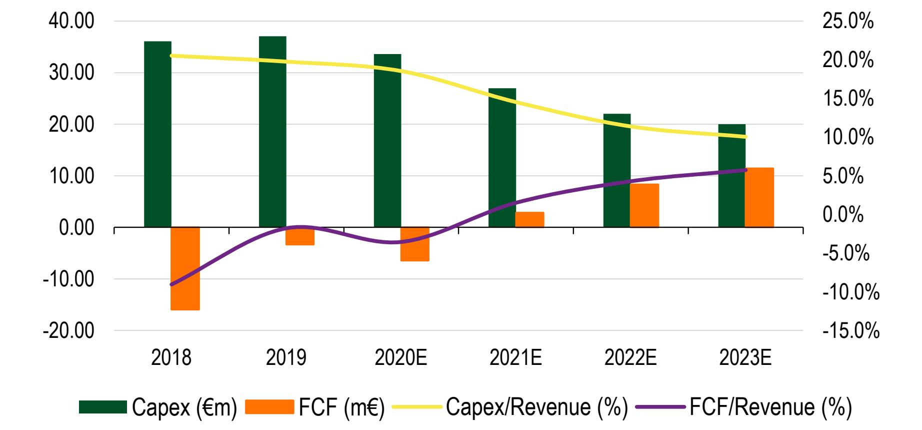
Source: Company data, MainFirst estimates

In addition to being a source of recurring revenue (invoicing spread over several years), the ramp-up of SaaS, in our view, should serve as a boost to the group's growth. The full price of the licence, under a subscription or rental model utilised by SaaS contracts, in our view, should be significantly higher than the price of the historic licences, since SaaS distribution methods are more conducive to cross-selling.

End of ERP investments drive FCF into positive territory

We see a shift in the cost structure of the business, partially driven by the increase in SaaS-based revenues, but also because of the end to a significant investment phase (e.g. developing its proprietary ERP system).

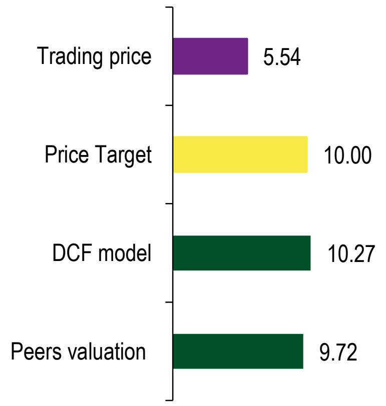
Figure 4: Return to positive Free Cash Flow



Source: Company data, MainFirst estimates

In addition to improving the operating margin, the return to a more normative level of investment (which we identify at around €20m) is forecast to drive cash flow into positive territory from 2021 onwards. This improvement in free cash flow is important as it helps to alleviate Prodware's high level of net debt, which is a key area of investor concern regarding. Here, the group's net debt stood at €83.2 million in 2019 (excluding IFRS16), or 2.3x EBITDA, limiting management's financial flexibility.

Figure 5: Valuation methods



Source: MainFirst Research

Valuation – relatively cheap for historic reasons but clear operational triggers to unlock value

High levels of capex, increasing indebtedness in recent years, and slower than expected conversion of the model towards SaaS have weighed on the stock. This, coupled with a small market capitalisation and low liquidity (despite >50% free float) explain, to some extent, why Prodware currently trades at such low multiples of 3.6x EV/EBITDA 21E (excluding IFRS 16). As indicated above, we believe those issues will be addressed in the coming semesters which should lead to a rerating. Nevertheless, we acknowledge that investors will want to see actual progress before agreeing to pay a full price for the shares, and hence we apply a 20% discount on our valuation methods to reflect these issues, which we may reassess depending on the group's progress.

Based on both our DCF model (€10.27 fair value per share), which captures the longer term prospects of the company, as well as our peer group valuation (€9.72 per share), the shares appear significantly undervalued. The average of these two metrics leads to our price target of €10.00, providing c.80% potential upside from current share price levels. Hence, we initiate coverage on Prodware with a Buy rating. Assuming Prodware delivers on the operational trends and based on our financial estimates, as outlined further on, we could see a re-rating of the stock.

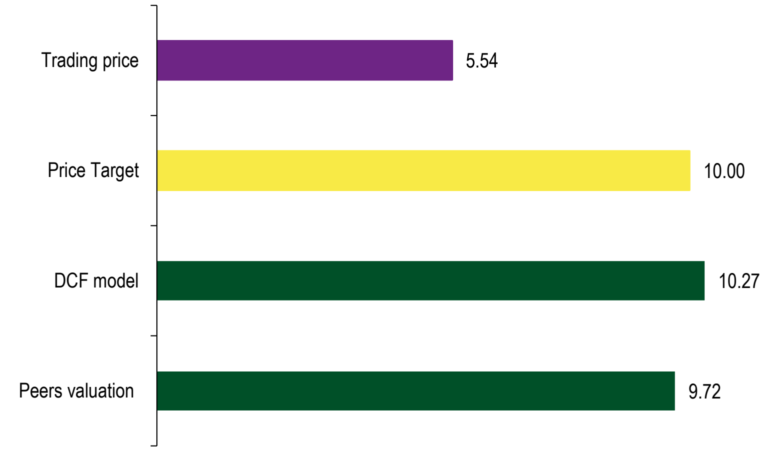
Contents

Valuation

Our price target of €10.00 is derived from the average of two valuation methods: a DCF model and a peer group comparison. With 80% upside potential from current share price levels, we initiate coverage with a Buy rating.

Summary and rating

Figure 6: Valuation methods



Source: MainFirst Research

High capex, increasing indebtedness in recent years, and a slower than expected conversion of the model towards SaaS have weighed on the stock historically. As indicated above, we believe those issues will be addressed in the coming semesters which should lead to a rerating. Nevertheless, we acknowledge that investors will want to see actual progress before agreeing to pay a full price for the shares, and hence we apply a 20% discount to our valuation methods to reflect these issues, which we may reassess depending on the group's progress.

DCF analysis

Our DCF based valuation uses forecasts up to 2030E and we have detailed financial estimates until 2022E (excluding IFRS16). We use a WACC of 8.7% and a terminal growth rate of 1.5%. Our WACC is based on the assumptions below:

- Risk-free rate: 1.0%
- Beta: 2.5
- Equity-risk premium: 6.0%
- Cost of debt: 4.0%
- Tax rate: 20.0%
- Percentage of financing represented by debt: 56.0%

This leads to a fair value per share of €12.84, and €10.27 after the application of a 20% discount.

Figure 7: Sensitivity analysis of DCF based fair value to WACC and terminal growth rate assumptions

	WACC										
	6.2%	6.7%	7.2%	7.7%	8.2%	8.7%	9.2%	9.7%	10.2%	10.7%	11.2%
0.5%	20.2	17.9	15.9	14.2	12.7	11.4	10.3	9.3	8.4	7.5	6.8
1.0%	21.9	19.3	17.0	15.1	13.5	12.1	10.8	9.7	8.8	7.9	7.1
1.5%	24.0	20.9	18.4	16.2	14.4	**12.8**	11.5	10.3	9.2	8.3	7.4
2.0%	26.6	22.9	19.9	17.5	15.4	13.7	12.2	10.9	9.7	8.7	7.8
2.5%	29.8	25.3	21.8	19.0	16.6	14.7	13.0	11.6	10.3	9.2	8.2

Source: MainFirst Research

Peer group analysis

Prodware, in our view, is the hybrid of a digital service company and a software publisher. Our peer group is a sample of small and mid-cap companies in the IT and software publishing sectors.

When applying peer multiples (EV/Revenue, EV/EBIT, P/E) to our estimates on Prodware we obtain a fair value of €12.15, and €9.72 after the application of a 20% discount.

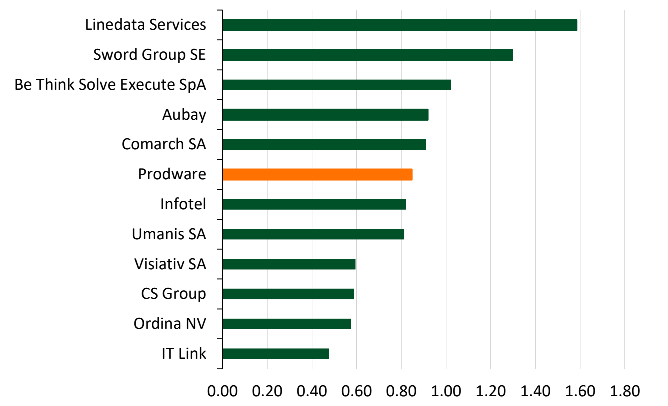
Figure 8: Peer group valuation

Priced at 19th october 2020		Price close (LocalCurn)	Mkt. Cap. (EURm)	Net Debt (EURm)	EBIT mgin (%)	EV/Revenue (x) 2021E	EV/Revenue (x) 2022E	EV/EBIT (x) 2021E	EV/EBIT (x) 2022E	P/E (x) 2021E	P/E (x) 2022E
Aubay	€	31.15	411	12	9.9%	0.92	0.9	10.5	9.9	15.7	14.7
Be Think Solve Execute SpA	€	1.12	151	13	8.0%	1.02	1.0	9.4	8.5	12.8	10.9
Comarch SA	PLN	197.00	351	-12	9.4%	0.91	0.9	9.5	9.4	15.0	15.0
CS Group	€	3.30	81	63	4.8%	0.59	0.6	11.2	9.4	8.8	4.4
Infotel	€	36.60	246	-57	9.0%	0.82	0.8	7.9	6.8	13.8	12.5
IT Link	€	10.30	18	6	6.6%	0.48	0.4	9.2	6.3	10.8	7.1
Linedata Services	€	27.50	182	89	18.1%	1.58	1.5	9.3	9.2	10.0	10.0
Ordina NV	€	2.29	214	13	5.9%	0.57	0.5	6.1	4.4	8.5	6.2
Sword Group SE	€	32.15	306	-51	9.6%	1.30	1.2	14.4	12.7	22.1	19.4
Umanis SA	€	6.32	117	81	6.1%	0.81	0.8	11.6	7.4	11.9	7.0
Visiativ SA	€	20.20	81	38	5.7%	0.60	0.6	9.4	7.3	12.7	9.1
Prodware	€	5.54	43	112	9.2%	0.8	0.8	8.6	7.5	4.1	3.4
Global peers average multiples						**0.9**	**0.8**	**9.8**	**8.3**	**12.9**	**10.6**
Valuation of Prodware based on peers						96.5	94.4	121.5	100.4	155.9	131.0
Average									**116.6**		

Source: Eikon Thomson Reuters (peers and prices as of close on 19 October 2020), MainFirst Research

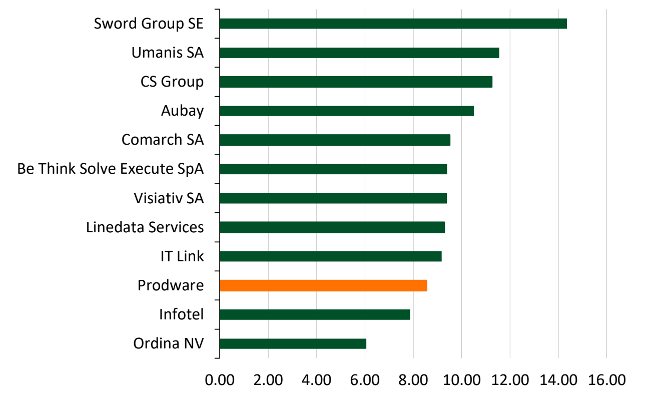
The group's financial situation, reflected in a net debt position (€83.2m in 2019, excluding IFRS16) is manageable in our view, but nevertheless limits management's flexibility. We believe this partly explains the historical discount to our sample of peers. The significant investments required for future growth, which in the case of the ERP investment we expect to end in 2021, also weighed on the group's results, in particular on cash flow, and subsequently the valuation multiple applied.

Figure 9: EV/Revenue multiples (2021)



Source: Eikon Thomson Reuters (peers and prices as of close on 19 October 2020), MainFirst Research

Figure 10: EV/EBIT multiples (2021)



Source: Eikon Thomson Reuters (peers and prices as of close on 19 October 2020), MainFirst Research

Significant employee share ownership

The group is active in terms of share buybacks. In 2019, the company repurchased 430,270 shares (representing 5.5% of the capital) at an average price of €8.54 (€3.67 million), which are currently held in treasury stock.

We note that there are many dilutive instruments which can be exercised. The most significant is the BSAANE warrants, providing the option to subscribe for and/or purchase new and/or existing shares. These represent 29% of the current capital, and are issued to members of the general management, employees, or corporate officers of the company and its subsidiaries.

Figure 11: Potential dilution from warrants offered to employees

Issue date	Type of securities	Maximum number of potential shares	Strike price	Maximum Maturity
Jun-15	BSAANE	265 000	€ 7.28	Jul-20
Mar-16	BSAANE	536 000	8,10	Mar-26
Apr-17	BSAANE	510 000	8,10	Apr-27
Jun-17	BSAANE	560 000	8,32	Jun-27
Oct-18	BSAANE	363 300	13,19	Oct-28
Total		**2 234 300**		

Source: Company data, MainFirst Research

In addition, preference shares, as well as ordinary shares, were also granted at no cost to members of the group. As of 31 December 2019, according to the projections for calculating the achievement of performance criteria, 343,000 ordinary shares could be issued.

Note that we have factored in a full dilution in our valuation methods above.

Prodware in a nutshell: a unique value proposition

Solid foundation of strategic partnerships supporting growth and technology

Prodware is a leading Microsoft partner in the EMEA zone thanks to the acquisition of the operations of pan-European integrator Qurius in 2011-12. Remarkably, the group is the only French company to be part of Microsoft's “Inner Circle” for Microsoft Dynamics business solutions, an accolade bestowed on just a dozen partners worldwide. The company also partners with other leading software providers, some of which are described below.

Prodware works with **Microsoft** to offer its customers management software solutions (Enterprise Resource Planning (ERP) and Customer Relationship Management (CRM)) which are adapted to clients’ business models by implementing and optimising Dynamics 365, Office 365, Azure, or Power BI applications. This partnership has allowed Prodware to obtain valuable certifications, such as ScoreFact, which is an independent certifier. These accreditations and certifications, in addition to its track record, add further credibility to Prodware’s ability to satisfy its clients’ needs. Prodware is ScoreFact certified with ERP systems including Microsoft Dynamics 365, Microsoft Dynamics 365 for Finance and Operations, and Microsoft Dynamics CRM. Furthermore, as mentioned, Prodware is a member of the Microsoft Inner Circle for Microsoft Business Applications.

We believe the company is well positioned to benefit from the structural growth led by Microsoft’s solutions. Our Stifel colleague, Brad R. Reback, who covers Microsoft, expects Microsoft’s top line to grow at a CAGR of 13% during FY20-23E, driven by its Commercial Cloud business which is forecast to grow at a CAGR of 28% during this period (Azure CAGR of 33%, Dynamics 365 up 40%, and Office 365 up 8%).

With the implementation of **SAGE** solutions, Prodware offers its customers commercial, financial and human resources management solutions for small and medium-sized companies. This alliance has also received ScoreFact certification with the SAGE FRR1000 Cloud Solution.

Prodware is an **Autodesk** Platinum Partner, which is highest accreditation offered by Autodesk. Together, Autodesk and Prodware offer consulting services in change management, training and technical assistance to customers equipped with Autodesk software.

Leveraging on both its strategic partnerships which provide access to leading and established technologies, as well as its know-how in terms of innovation, Prodware develops its own software to offer customised solutions. These have helped to establish the company as a key strategic partner for its clients.

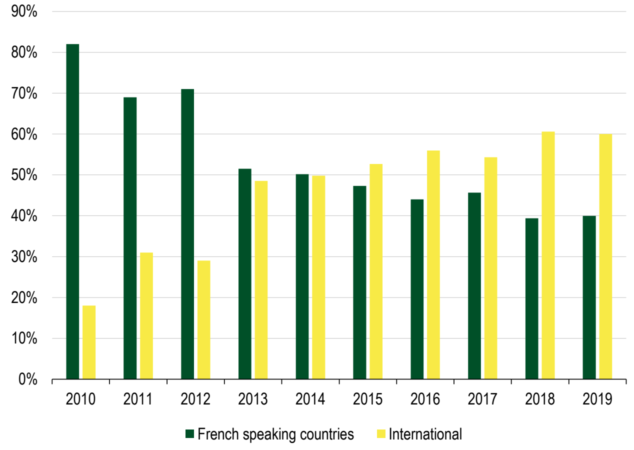
Healthy mix of its core French operations and international exposure

Ability to support customers in over 75 countries

Over a number of years, Prodware has strengthened its regional and international footprint to offer a responsive local service to over 19,000 customers. With a presence in 13 countries, the group benefits from an efficient organisation able to support the international expansion of its customers. With the inclusion of partnerships and strategic alliances, Prodware is able to operate in more than 75 countries. Note that Prodware’s international activities represented 49% of sales in 2013, rising to 60% in 2019.

However, the impact of the COVID-19 pandemic has driven Prodware to focus on consolidating its geographical positions in Europe, targeting areas where the potential for profitable growth is most significant. This is why the group has announced the disposal of its business unit in Tunisia, as well as the signing of an agreement to sell its subsidiary in Israel (except the Research and Development Centre of Prodware Israel and the 365x Scaler).

Figure 12: Split of revenues between French-speaking countries and International (2010-19)



Source: Company data

Customer-centric strategy

Prodware does not limit itself to the integration of solutions, rather it works alongside clients to find strategic solutions to their business challenges. In addition to support for international deployments, the group offers a range of processes and monitoring services covering the entire lifecycle of the services provided. Its maintenance activities are also an asset and, in our view, a proven differentiating factor. These maintenance activities cover the following areas:

- Multilingual user support
- Preventive and corrective maintenance
- Evolutionary maintenance
- Management of the service provided

Experienced management team

Based on our assessment, the management team appears to be strong a complementary skills set. Moreover, it is in tune with the sector, in terms of both skills and experience. Key management members are detailed below.

Philippe Bouaziz is the co-founder, former CEO, and current chairman of Prodware. Mr Bouaziz has degrees in software engineering, network & system operation research, and has a PhD from the Université Pierre et Marie Curie. He began his career in the R&D and Support departments of the multinational, Texas Instruments. He then became a consulting manager for a financial IT software creator before subsequently founding Prodware. Mr Bouaziz's ambition for Prodware is to become a global leader in computer sciences and to further develop access to innovative and quality services for its clients on a global scale.

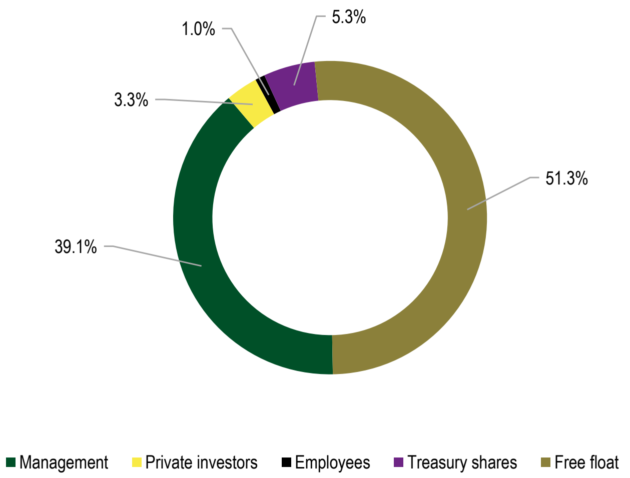
Alain Conrard is the CEO of Prodware. Prior to his current post, Mr Conrard spent most of his career in the IT sector. He obtained a degree in computer science at the Institut Universitaire de Technologie and a degree in company management at Institut d'Administration des Entreprises. After his graduation, Mr Conrad held various positions, such as regional director and consultant for an IT company. From 1994, he was a mid-market marketing manager for Sage, the accounting software firm, where he stayed until 2003 when he was appointed CEO of Prodware.

Stephane Conrard is the CFO and deputy managing director of Prodware. Mr Conrard holds a bachelors degree in eastern civilization and languages as well as a diploma in public accounting. Stephane Conrard began his career working in accounting, auditing and consulting for large firms like PricewaterhouseCoopers (PWC) and Organization, Consulting, Audit (OCA). In addition, he created two accounting firms in 2001, five years before joining Prodware in 2006 as a CFO.

Source: Prodware

Shareholder structure

Figure 13: Management team holds a significant stake but free float is high



Source: Company data, MainFirst Research

30 years of expertise

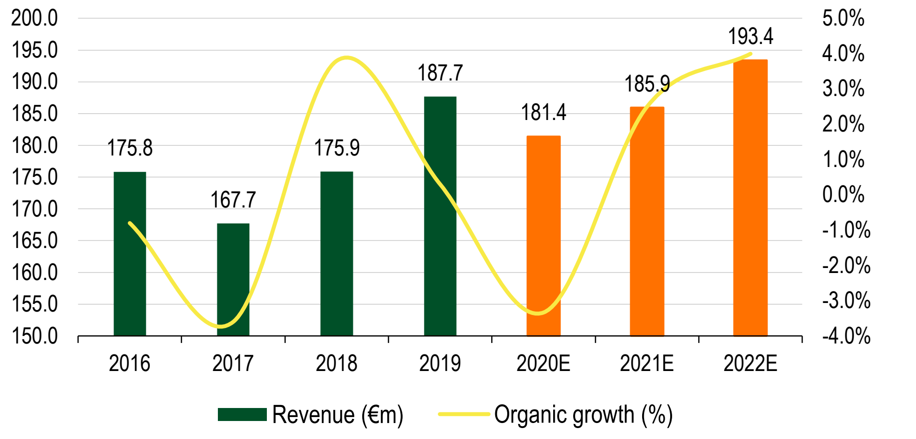
Figure 14: Key dates in Prodware's history

Source: Company data, MainFirst Research

Growth powered by digital transformation and shift to SaaS

At the crossroads of technology and consulting, the group assists its clients throughout their transformation project, optimising processes through tools customised to their needs, while ensuring successful completion of the project. Overall, in our view, the current unprecedented health crisis could accelerate awareness and accentuate the digital needs of small and medium-sized enterprises, both in France and internationally. After an exceptional 2020, we are confident in Prodware's ability to deliver organic growth of 2.5% in 2021 and 4% in 2022, despite the difficulties associated with the transition from the legacy licence into the SaaS-based system.

Figure 15: A unique value proposition to support digital needs



Source: Company data, MainFirst estimates

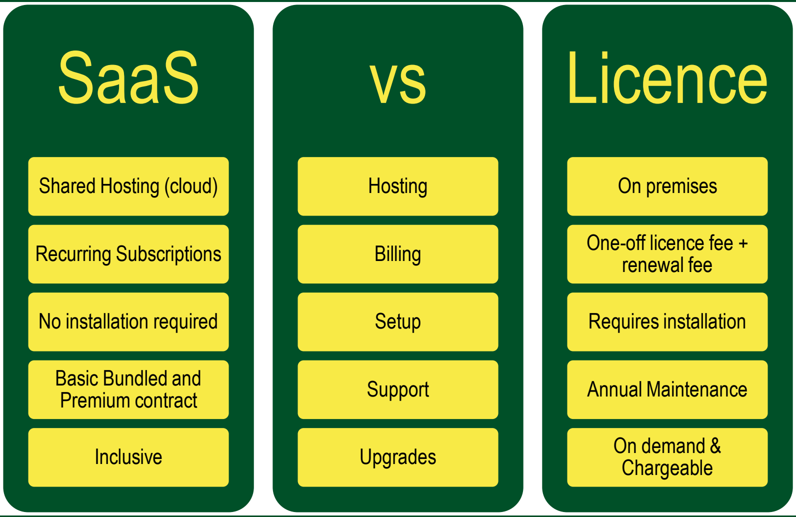
Gradual transformation of business model towards SaaS

The definitive success of the SaaS model

According to Synergy Research, based on 2019 figures, the total enterprise software market exceeded US$450bn, of which 23% was SaaS. This compares to less than 2% in 2009. Using Microsoft as an example, total software revenues have doubled since 2009, reaching more than US$100bn, during which time Microsoft's SaaS revenues have increased from zero to more than US$20bn.

SaaS offers customers applications in the form of online services on a pay-per-use basis. Access to the applications is done remotely. The major benefit, thanks to SaaS, is that clients no longer toned to make heavy investments in infrastructure and licences to use the software, thereby reducing their financing needs.

Figure 16: SaaS vs Licence



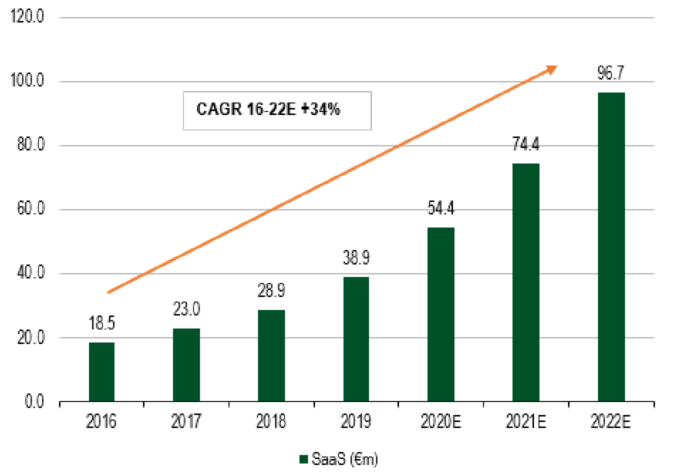
Source: MainFirst Research

Adaptability, accessibility and attractive prices constitute the main features of the SaaS model

Prodware is capitalising on the evolution of software consumption patterns, as characterised by the rise of the SaaS model. A major part of this rise, in our view, has been driven by Microsoft, which is increasingly marketing its solutions in this way.

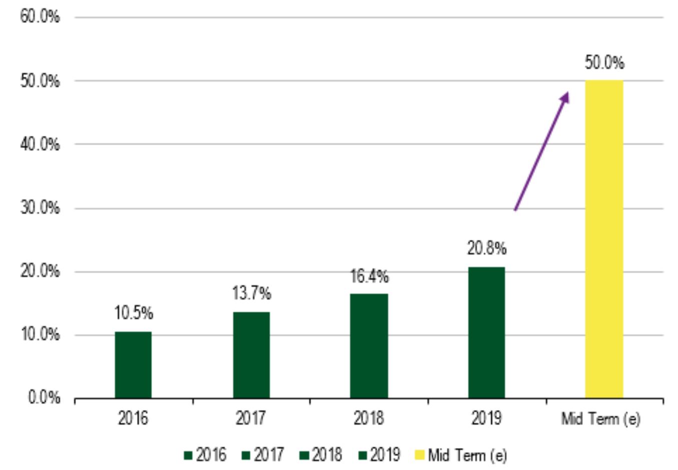
More specifically for Prodware, its SaaS related sales reached €38.9 million in 2019, reflecting strong y/y growth of 34.8% and representing 20.8% of total sales, which is materially up from levels of 10.5% in 2016. We forecast that SaaS sales could represent up to 50% of revenues in the medium term.

Figure 17: SaaS, impressive rise …



Source: Company data, MainFirst estimates

Figure 18: … and a significant proportion of revenues



Source: Company data, MainFirst estimates

Unlike the traditional perpetual licence sales which are one-off in nature, these SaaS sales, combined with the addition of maintenance contracts, generate attractive recurring revenues for the group. Together these represented 38% of revenues in 2019. SaaS contracts are multi-year. Invoicing that was previously done in one go will now be spread over several years. Note that the full price of the licence for a subscription model should eventually be significantly higher than the price of a one-off licence, since this distribution method is more conducive to cross-selling of other software solutions and services.

Virtuous circle of SaaS: higher margin ahead

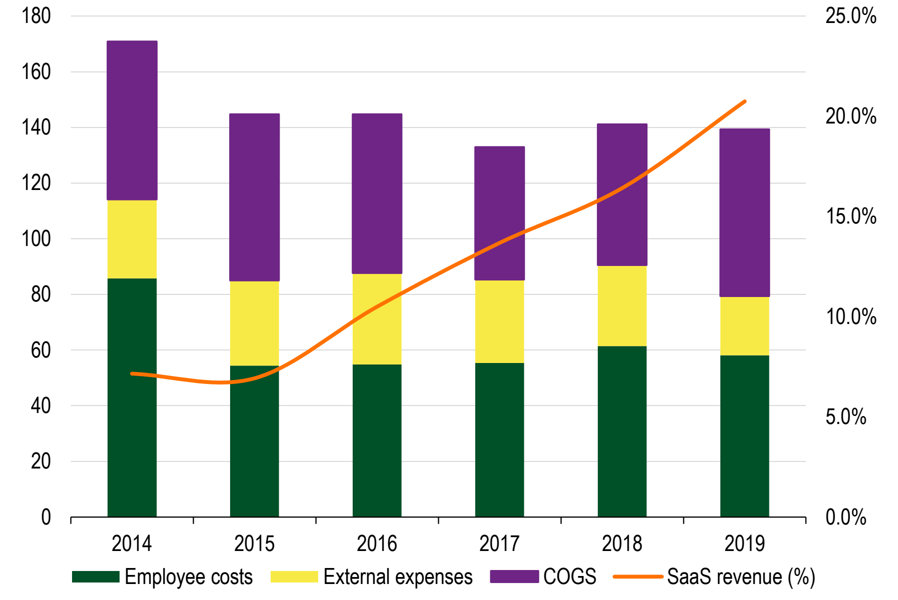
Despite the cannibalisation of sales resulting from the shift towards more SaaS sales, which partly explains the group's more modest organic growth in recent years, we believe the rise of SaaS will increasingly motivate the group's growth.

This change, which has been underway for several years, has necessitated investments and reorganisations within the group. However, the rise of SaaS should contribute to a reduced cost structure and thus increase profitability longer term.

In addition to being more sustainable, the revenue generated by SaaS and hosted solutions is more profitable. The transition from 'on premise' software consumption (purchase of licences) to 'on demand' consumption (rental) is an opportunity for the hosting company to cross-sell a range of ancillary services inherent in this form of revenue model. Moreover, remote distribution with monthly invoicing makes it easy to test new solutions, which often encourage impulse purchases, as well as providing the ability to cut off the service remotely in the event of non-payment. The pooling of resources and infrastructures also optimises the cost borne by the hosting providers, which ultimately makes it possible to generate significantly higher margins for on-demand offers than for on-premise offers.

An increase in SaaS sales should also result in better control of COGS as well as personnel expenses, thus improving profitability

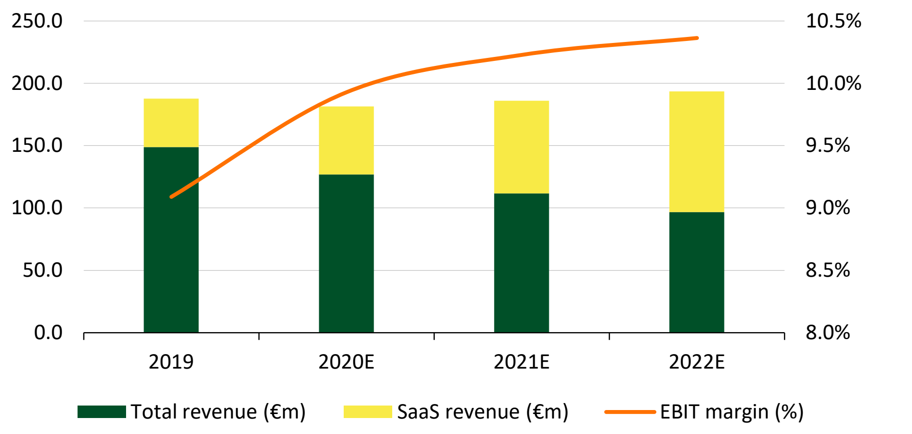
Figure 19: A better controlled cost structure with the rise of SaaS (€m)



Source: Company data, MainFirst Research

The shift to SaaS-based sales has been ongoing for number of years, but we see the indirect implications of the COVID-19 pandemic on corporate operations, investment priorities and remote working, as accelerating this trend. We cautiously model a 150bps increase in EBIT margins between 2019-22E as the proportion of SaaS revenues increases from 30% to levels of up to 50%.

Figure 20: The virtuous circle of SaaS – revenue split (€m) and EBIT margins

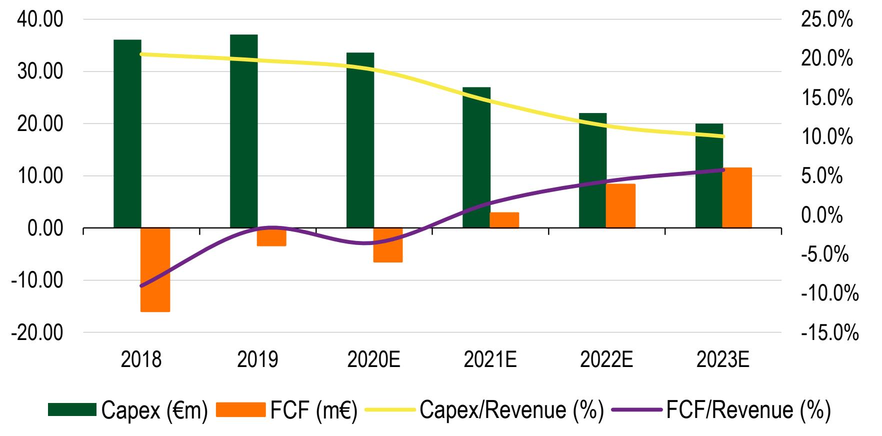


Source: Company data, MainFirst estimates

Return to a normative level of capex will drive FCF improvement

In addition to the ramp-up in SaaS based revenues, the end to a significant investment phase (e.g. developing its proprietary ERP system) in 2021 should enable Prodware to generate positive free cash flow from 2021 onwards. The group has developed its proprietary ERP system for an incremental investment of around €25m over three years. Prodware should subsequently return to a more normative level of investment (which we identify at around €20m).

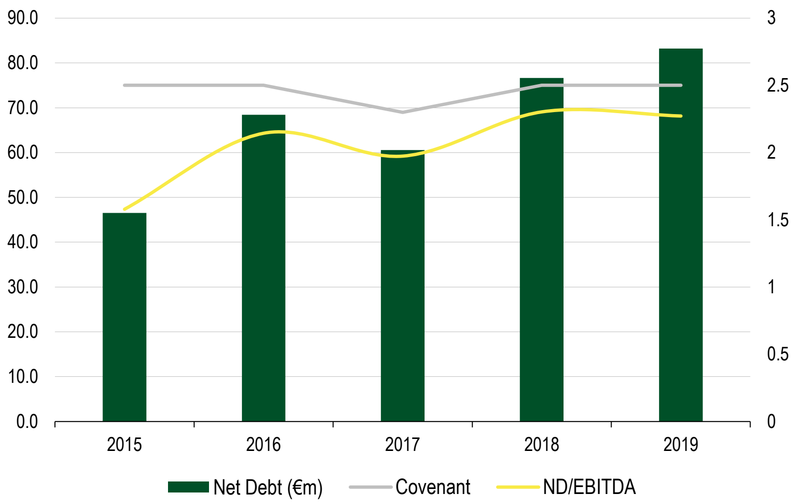
Figure 21: The end of ERP investments to drive FCF into positive territory



Source: Company data, MainFirst estimates

This improvement in free cash flow is important as it would help to potentially reduce Prodware's high level of net debt, which is a key area of investor concern. More specifically, the group's net debt was €83.2m at the end of 2019 (excluding IFRS16), representing 2.3x EBITDA, limiting management's financial flexibility.

Figure 22: Trend in net debt (€m) and leverage ratio compared to covenants



Source: Company data, MainFirst Research

Financial estimates

Revenue and earnings model

Note that the level of capitalised R&D almost doubled in one year, from €11.8m in 2018, to €23.4m in 2019, thus improving the EBITDA margin by approximately 600 basis points. This amount will be expensed as it is amortised over time.

In addition, Prodware has adopted a cautious approach to research tax credits, which represents 3.1% of revenue (vs 6.3% in 2016).

Profit & loss account

Figure 23: P&L

YEAR TO DECEMBER (EUR) PROFIT & LOSS ACCOUNT	FY-18	FY-19	FY-20E	FY-21E	FY-22E
Group revenue (as reported)	175.9	187.7	181.4	185.9	193.4
EBITDA	33.3	48.3	47.8	48.3	49.0
EBIT	17.2	17.3	18.2	19.2	20.3
Pre-tax result	8.9	10.8	12.9	14.0	15.0
Income tax, other items	0.3	-0.8	-0.9	-1.3	-2.0
Net result group	9.1	10.5	12.2	12.7	13.1
Minorities, other	0.1	-0.1	0.1	0.1	0.1
Net result shareholders	9.2	10.4	12.3	12.8	13.2

Source: Company data, MainFirst estimates

Cash flow and balance sheet

Figure 24: Cash flow statement

YEAR TO DECEMBER (EUR) CASH FLOW STATEMENT	FY-18	FY-19	FY-20E	FY-21E	FY-22E
Net profit	9.2	10.4	12.3	12.8	13.2
Non cash items and others	13.9	20.0	17.4	17.3	17.6
Cash flow	**23.1**	**30.4**	**29.6**	**30.1**	**30.8**
Effect of change in working capital	-3.0	3.3	-2.5	-0.3	-0.5
Net operating cash flow	**20.1**	**33.7**	**27.1**	**29.8**	**30.3**
Capital expenditure (intangibles, tangibles)	-36.1	-37.0	-33.6	-27.0	-22.0
Free Cash Flow	**-15.9**	**-3.3**	**-6.5**	**2.8**	**8.3**
Net cash flow allocated to investing activities	0.0	0.1	0.0	0.0	0.0
Net cash flow from financing activities	19.7	-4.8	-0.2	-0.3	-0.4
Change in net cash	**3.7**	**-8.1**	**-6.7**	**2.5**	**7.9**

Source: Company data, MainFirst estimates

Figure 25: Balance sheet

YEAR TO DECEMBER (EUR) BALANCE SHEET	FY-18	FY-19	FY-20E	FY-21E	FY-22E
Fixed assets	**206.2**	**254.4**	**254.4**	**254.5**	**254.8**
t/o Goodwill	34.6	34.6	34.6	34.6	34.6
Curent assets	**110.1**	**105.4**	**97.6**	**101.5**	**111.5**
t/o Inventories	0.1	0.1	0.1	0.1	0.1
t/o Trade receivables	58.0	53.2	52.2	53.5	55.6
Group equity	**138.2**	**144.8**	**159.1**	**172.6**	**186.3**
t/o Shareholders' equity	137.6	144.4	158.5	172.0	185.6
Interest-bearing liabilities	**87.4**	**104.9**	**104.9**	**104.9**	**104.9**
Other liabilities and provisions	**90.6**	**110.0**	**88.0**	**78.4**	**75.0**
t/o Pension provisions	4.3	5.7	5.7	5.7	5.7
t/o Trade liabilities	20.7	23.6	27.7	24.0	21.1
Balance sheet total	**316.2**	**359.8**	**352.0**	**356.0**	**366.3**
Net working capital	13.7	9.6	12.1	12.4	12.9
Capital employed (incl. Goodwill)	214.8	257.6	278.5	289.6	295.3
Net debt	76.6	112.8	119.4	116.9	109.0

Source: Company data, MainFirst estimates

The group applies IFRS 16 as from 1st January 2019 under the simplified retrospective method, without restatement of previously published figures. The Group is lessor to its offices in France and abroad and has taken out leases that fall within the scope of IFRS 16 for its vehicle fleet, its IT equipment and its hosting service contracts. Under IFRS 16, all leases are now recognised as assets through the recognition of a right of use and as liabilities through the recognition of a liability equivalent to the present value of future payments.

Figure 26: Application of IFRS 16

YEAR TO DECEMBER (EUR) BALANCE SHEET	FY-18	FY-19	FY-20E	FY-21E	FY-22E
Debt	88.5	116.6	116.6	116.6	116.6
Cash and cash equivalent	11.9	3.8	-2.9	-0.4	7.6
Net debt	**76.6**	**112.8**	**119.4**	**116.9**	**109.0**
Application of IFRS 16	*0.0*	*29.6*	*29.6*	*29.6*	*29.6*
Net debt (excluding IFRS 16)	**76.6**	**83.2**	**89.9**	**87.4**	**79.4**
EBITDA	**33.3**	**48.3**	**47.8**	**48.3**	**49.0**
Application of IFRS 16	***0.0***	***11.7***	***11.7***	***11.7***	***11.7***
EBITDA (excluding IFRS 16)	**33.3**	**36.6**	**36.1**	**36.6**	**37.3**
Net debt / EBITDA (excluding IFRS 16)	**2.30**	**2.27**	**2.49**	**2.39**	**2.13**

Source: Company data, MainFirst estimates

We note that in 2016, Prodware subscribed to a Euro PP loan for €79m, which was intended to finance the development and refinancing of existing debt at a lower cost. Subsequently, in July 2018, the group's bond and bank debt was refinanced in order to support the organic and external growth policy and to benefit from a new maturity. A new bank loan was arranged for €92.5 million, most of which is repayable at the end of years six and seven, i.e. 2024 and 2025, for €62.5 million.

Risks

COVID-19 impact

The COVID-19 pandemic has had significant economic consequences. The IT sector in which Prodware operates is particularly sensitive to any such fluctuations that might impair or delay the investment capacity and/or solvency of Prodware's clients. Moreover, the countries in which Prodware operates have each been affected by the pandemic differently and government aid varies widely between geographies. Having been unable to provide a reliable outlook, Prodware management is keeping a close eye on the progression of the pandemic and remains confident in the fundamentals of the business model.

Competition

There is a high degree of competition for IT partners who provide digital transformation support, sometimes leading to significant price pressure. In order to distinguish itself, Prodware deploys a comprehensive offer which is focused on innovation and customer support, with an end-to-end offer integrating the entire value chain. However, this does not prevent the risks associated with the emergence of the competition who are aggressive on pricing and could lead to market share losses for Prodware.

Risks from external growth transactions

In line with its business strategy, Prodware regularly makes targeted acquisitions of companies or complete business segments. Failure to properly identify and integrate acquisition targets may result in lower than expected profitability. This may negatively impact the Group's results and financing requirements.

Human resources

Prodware operates in a very tight market for certain skills. Competition to attract and retain the best employees is high. Therefore, the group cannot rule out the possibility of tensions sometimes arising in terms of recruitment and/or departures of its skilled employees. This could have an effect on the group's ability to deliver projects on time or on commercial terms.

Balance sheet

Prodware's debt is subject to compliance with ratios and covenants in accordance with usual practices. Compliance with these ratios is subject to the certification by the Statutory Auditors at the time of their audit of the financial statements for the year to 31 December. The group does not expect any difficulty in complying with these covenants.

Appendix

Clear focus and care for employees

A commitment to increasing its appeal to potential employees

In the context of business growth, digital service companies have specific needs in terms of manpower, particularly requiring young qualified employees. According to the KPMG-Syntec Digital survey In 2018, 71% of digital companies expressed recruitment difficulties. AI engineers, cybersecurity analysts, data scientists, etc. are all in high demand. As a result, personnel costs have become the main drivers of expenditure for digital services companies; over the last five years, they have accounted for more than half of the revenues for digital companies, according to Xerfi.

Prodware's strategy on human capital is measured against these three objectives; 'Improving the Group's attractiveness', 'Developing the Group's talents', and 'Building employee loyalty'.

Development of the employer brand is one of the Prodware's priorities. The Group naturally draws on social media to relay company news, job offers and key events. Prodware France was ranked amongst the 500 best employers in a survey run jointly by business magazine, Capital, and online statistics portal, Statista. They were also ranked fourth place among software publishers.

Prodware considers training a priority, putting in place an internal training school called the Prodware Academy so that participants can gain technical skills in the group's business lines or solutions. Employee mobility is also encouraged, with a constant flow of information about various internal opportunities.

In order to improve employee quality of life at work, Prodware's head office was overhauled in 2019, with numerous collaborative tools made available to employees. Prodware also introduced a group Intranet in all countries, enabling the smooth interaction and flow of information among all employees.

In recent years Prodware has tightened its remuneration structure, emphasising the variable portion connected with the achievement of qualitative and quantitative objectives. In December 2016, preference shares were allocated to more than 100 employees (see valuation section).

With the COVID-19 pandemic related crisis, tensions in the labour market, which have been particularly high in recent years, could subsequently ease. This could benefit the group in the context of an upturn in activity. At the same time, Prodware rigorously manages its costs, restricting expenses to strategic investments to preserve its profitability. Short-time working measures have been implemented, as well as a halt to all investments not necessary for the activity (including recruitment).

Product and service offering

Consulting, publishing and IT integration services

Prodware supports the SMEs and subsidiaries of major groups throughout their digital transformation thanks to sector-specific business solutions. Focused on what it does best, the group concentrates on the following sectors of activity:

- **Distribution**
- **Manufacturing**
- **Professional services**
- **Retail**

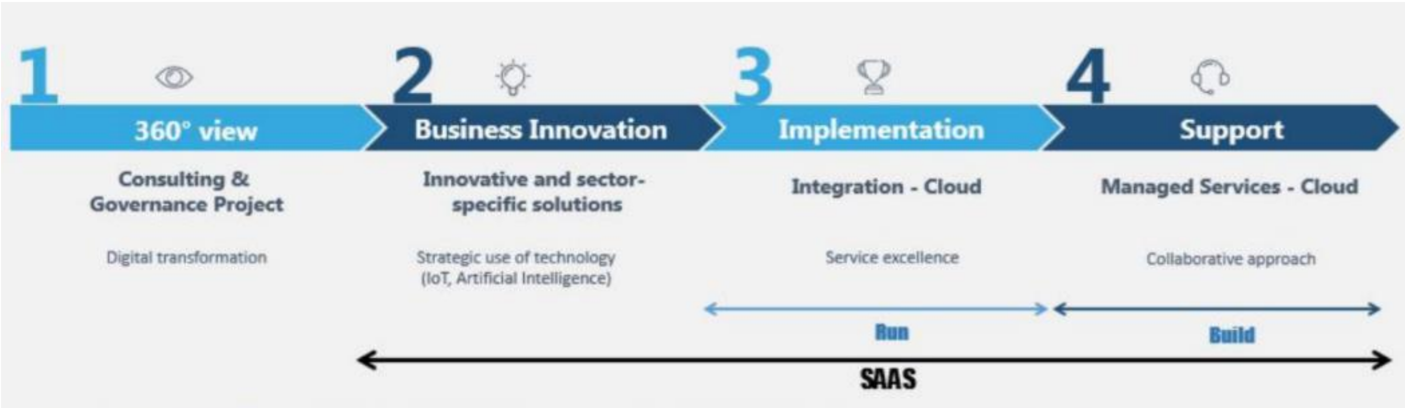
At the crossroads of technology and consulting

The Prodware offer, in line with market expectations, is structured around four key pillars:

- **Consulting** on information technologies and more specifically on Innovation;
- **Publishing** of industry-specific solutions and innovative business lines
- **Implementation** of these solutions for its clients
- **Managed Services**, which keeps its clients' operations running 24/7

What sets Prodware apart, in our view, is that it has the ability to accompany its customers from end to end, throughout their digital transformation.

Figure 27: Agility & Innovation



Source: Company data

R&D driven innovation is in Prodware's DNA

A powerful R&D structure which supports the strategy

Beyond the classic integrator's activity, innovation is at the heart of Prodware's its strategy, enabling it to offer tailor-made solutions with higher added value. Customisation of the tools to adapt them to the company's specifications and needs is key. The group thus offers its own software solutions which are developed in-house (representing one third of activity). These are dedicated to specific needs in identified business sectors.

The group invested €22.3 million (approximately 12% of sales) in R&D in 2019 and devoted significant financial and human resources to innovation. An additional effort has been made with the development of a proprietary Enterprise Resource Planning (ERP) tool, which should also be part of the group's offer and could boost sales in the mid-term, in our view.

Figure 28: Technologies offered by the group

Source: Company data

A “win-win” approach for ambitious and sustainable business development

Prodware has a dedicated division for innovation, namely Innovation & Business Solutions (IBS), which nurtures start-ups focused on developing innovative business solutions. This enriches Prodware's catalogue of offerings and, in our view, provides real added value. This programme helps start-ups organise themselves around a development strategy while providing them with access to the distribution and sales channels of programme sponsors. In return, these solutions can be incorporated into the product catalogue and benefit from the “go-to-market” strategy of said sponsors, including Prodware.

The group is continuing its efforts in innovation, developing specific solutions to adapt its world leading solutions to customers’ needs.

Main competitors

Aubay is a French IT services company founded by Christian Aubert in 1998. The group assists companies in the transformation and modernisation of information systems in all sectors. The majority of Aubay's turnover comes from major banks and insurance companies (80% of French turnover and 66% of total European turnover).

Be Think, Solve, Execute SpA (Be group), founded in 1987, is an Italian IT consulting firm specialising in the Financial Services sector. Be group supports international finance and insurance institutions to create value and boost business growth.

Comarch SA is a multinational software house and systems integrator based in Kraków, Poland. Comarch provides services in areas such as Telecommunications, Finance and Banking, the Services Sector and to Public Administration.

CS Group is a French IT services company. The company designs information systems, develops and integrates software, manages projects and deploys industrial applications and provides science, technology and consulting services.

Infotel, founded in 1979, provides corporate digital transformation services and is present through 16 agencies throughout France and Monaco. In Europe, the group is continuing its deployment in the UK, Germany and the Benelux countries, as well as the US with its software division. The group assists clients in managing their digital resources, offers IT support and provides teams with advice.

IT Link is a French digital services company that specialises in Connected Systems. The group supports major operators in several sectors including Automotive, Energy, Aerospace, Defence, Telecoms, Media & Entertainment, Retail/Services, Health and Public transport.

Linedata is a French software company that offers a combination of technology and human resources to provide asset management, insurance and lending professionals with global solutions. Linedata has 20 offices and more than 700 clients in 50 different countries.

Ordina NV is a leading provider of consulting, solutions and IT services to the Benelux countries. With around 2,650 employees, Ordina supports clients in financial services, general industry, and the public sector.

Sword Group SE is an international consulting, services and software company which supports global leaders in their digital & technology transformation. Sword Group offers its clients comprehensive and integrated solutions on both strategic approach and execution.

Umanis SA is a French digital services company and operates in over 10 countries worldwide. It has partnerships with leading software companies such as Microsoft, SAP, IBM as well as Talend, Informatica and Tableau.

Visiativ SA is a French IT services company with multiple areas of expertise (consulting, software editing and integration, platform creation, and IT outsourcing). Visiativ has over 1,000 employees which cover business hubs across France. The group also has operations worldwide.

Market drivers

Digital transformation – a key challenge for companies

According to a report by Grand View Research in May 2020, the global digital transformation market was estimated at US$284.4bn in 2019 and is expected to reach US$1.17 trillion by 2027, representing a CAGR of 22.5% over the forecast period 2020-27

Looking at implementation rates at corporates, according to a Markets and Markets report, digital transformation is defined as a growth driver for 94% of the medium-sized companies surveyed, and 56% considered digital transformation an opportunity. Furthermore, 44% of the companies who carried out digital transformation processes reported an increase in (operating) efficiency, while 41% of the companies experienced better customer relations thanks to the new communication channel.

More and more companies are incorporating new technologies across their operations in order to optimise their revenue and growth profiles and to distinguish themselves from their competitors. As an illustration, it was found that 91% of small companies are willing to start their digital transformation. However, 34% of management teams at small companies find the digital transformation process complicated.

Furthermore, note that France is still lagging behind its main European partners in terms of digital technology, occupying 15th place out of 28 in the DESI 2020 European ranking according to digital competitiveness. There is clearly some catching up to be done here.

COVID-19 as a catalyst for accelerating digital transformation

The COVID-19 pandemic is having an impact on growth in IT investment, but, according to market intelligence provider International Data Corporation (IDC), many business opportunities remain. Interviewed companies have stated that they are ready to increase their investments in the Cloud, artificial intelligence (AI), and the internet of things (IoT). These three areas are arguably key to managing the economic consequences of COVID-19 and for clients to get back on the path of growth.

"The cloud appears to be resilient, with some companies continuing to increase spending while others focus on ways to reduce costs in the short term," said Stephen Minton, vice president of IDC Customer Insights & Analysis.

The COVID-19 pandemic-related crisis had a direct impact on client behaviour, with many asking to extend their payment terms, putting IT companies in a difficult situation in terms of cash and sustainability.

A consciousness emerged: digitalisation is now the priority

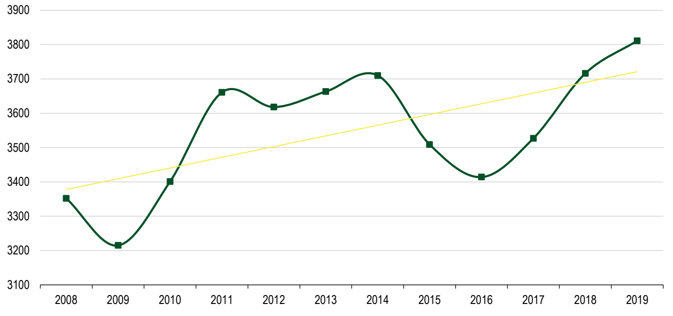
While the COVID-19 pandemic caused significant disruption to corporates, it also acted partially as a catalyst for companies to focus their investments on a “digital-first” basis. Cloud solutions, sharing documents, video conferences, security of information and tools available from remote locations were all prioritised. Companies realised that digitalisation was key to maintaining their activities and operations during the lockdown.

One of the notable benefits of the COVID-19 related lockdowns has been the ability of employees to work successfully from home. Companies increasingly understand that employees can word efficiently from home with the right technology.

Spending on the global IT market

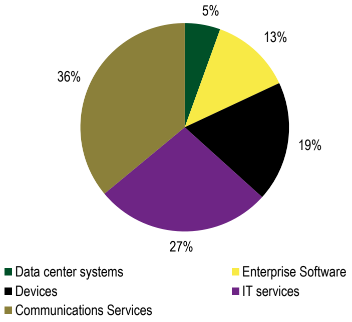
In 2019, the global IT spending market grew by around 2.3%, to €3.8trn, despite strong economic uncertainties. Growth was mainly driven by the enterprise software (+11.7%) and the IT services segments of the industry (+4.8%).

Figure 29: Spending on the global IT market (US$trn)



Source: Gartner, MainFirst Research

Figure 30: Breakdown by segment in 2019

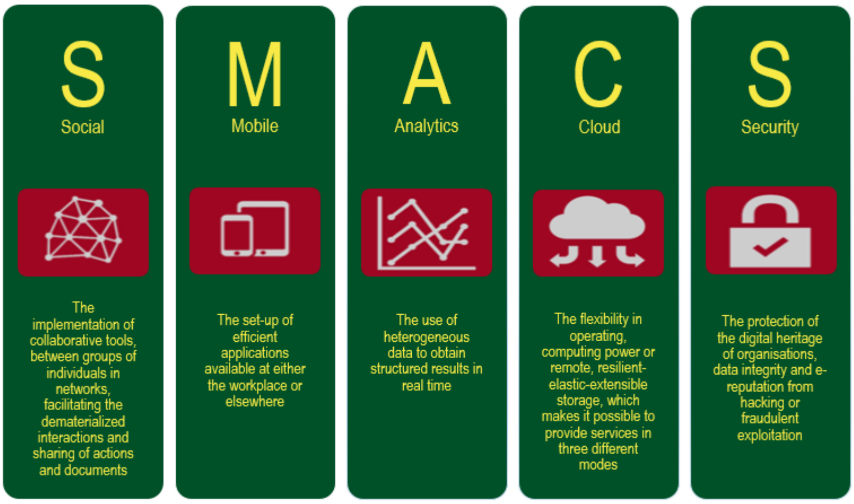


Source: Gartner, MainFirst Research

SMACS boosts growth: focus on cloud computing

Growth in the aforementioned enterprise area is driven by the technologies united under the acronym "SMACS". SMACS transforms uses by using (S)ocial networks, (M)obile services, large scale data exploitation "big data & (A)nalytics", (C)loud and (S)ecurity to meet competition and digital transformation challenges.

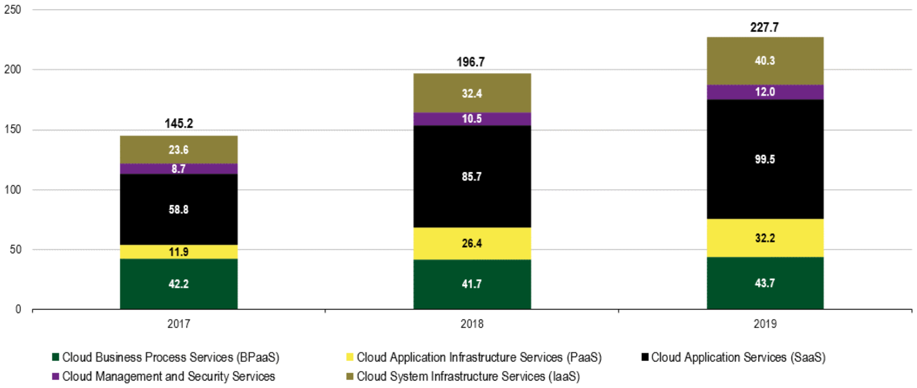
Figure 31: Social, Mobile, Analytics, Cloud, Security (SMACS)



Source: MainFirst Research

Focusing on Cloud Computing, according to Gartner, the global cloud market reached US$227.8bn in 2019, representing growth of 15.8% y/y.

Figure 32: Worldwide Public Cloud Services Revenue (USDbn)



Source: Gartner, MainFirst Research

Cloud computing allows companies and institutions to benefit from IT resources without having to maintain expensive servers and equipment themselves. In the so-called 'public' cloud, operators offer 'virtual machines' for rent, where computing capacity runs on a system of completely shared physical servers. There is also a 'private' cloud, where operators rent specific physical machines, and where the sharing remains internal to the company and its various departments. The services offered are varied: in some cases, customers only rent the capacity to use a given software (SaaS, software as a service), and in other cases, customers rent infrastructures or ‘virtual machines’ on which they install their own operating systems and software (Infrastructure as a Service, or IaaS).

Cloud computing, in our view, is the answer to digital transformation. IT is facing new challenges mainly due to the acceleration of the upheavals caused by the increasing evolution of technology.

Companies clearly see the cloud as a driver of digital transformation and a technology that supports businesses. With COVID-19 leading to many employees working remotely, tasks are being performed directly on an infrastructure deployed in the Cloud. Collaborative tools, such as Microsoft Teams and Google Meet, have become a critical part of the enterprise cloud ecosystem.

AI, Big Data and IoT stand out from the competition

Artificial intelligence, Big Data analysis, and the Internet of Things will be differentiating elements among leading cloud service suppliers. The number of connected devices is growing dramatically and is expected to reach US$50bn, according to Forrester Research. However, the technical limitations of high-speed networks could hamper their development. Edge computing now offers the opportunity to solve this problem through a paradigm shift in the world of cloud computing.

Rather than transferring data generated by devices connected to IoT networks in the Cloud or a data centre, edge computing allows data to be processed at the edge of the network directly where it is generated. However, while edge architecture is an alternative to the Cloud, it is not intended to replace it or compete with data centres, but to extend the ecosystem.

The development of artificial intelligence within corporates is rising rapidly. Today, 75% of companies worldwide are exploring or developing processes related to artificial intelligence, a trend which looks set to accelerate, in our view. If AI continues its democratisation as experts predict, this technology will be present in 80% or even 90% of companies by 2022, according to IBM research. SMEs could be the first to be concerned by this major change, according to Microsoft.

By the end of 2020, according to Forrester Research it is estimated that conversational AI will still account for less than 20% of customer service interactions. It is also estimated that 25% of Fortune 500 companies plan to automate certain tasks through the use of AI. For example, companies will use text analysis and machine learning when implementing certain automated robotic tasks. AI will be used to establish automatic responses or chatbots. However, due to the large number of customers who do not find a satisfactory solution when using chatbots, ultimately requiring the intervention of a person, the development of human skills will be required by companies. Thus, a balance will have to be found between the development of AI and the problematic issue of recruitment.

While forecasts at the beginning of the year predicted a 3.4% increase in 2020, Gartner expects global IT spending to fall by 7.3% in 2020 (representing US$3.5trn), reflecting the impact of the COVID-19 pandemic. All segments will experience a decline in 2020, with devices and data centre systems recording the biggest spending cuts. CIOs seek to optimise costs and will favour investments that ensure the smooth running of the business, to the detriment, at least in the short term, to projects and initiatives related to growth or digital transformation.

However, as the COVID-19 pandemic stimulates teleworking, sub-segments such as Public Cloud services stand out in the forecast, with growth of 19% in 2020. Cloud-based telecommunications and messaging, and cloud conferencing will also see high spending levels, growing by 8.9% and 24.3%, respectively according to Gartner.

The recovery of IT spending will be slow throughout 2020, with the hardest hit sectors, such as entertainment, air transport and heavy industry, taking more than three years to return to 2019 IT spending levels. At this stage, growth is clearly expected to pick up again in 2021, without catching up to 2019 levels. However, improved visibility over the medium term could raise awareness, leading to an acceleration of digital transformation projects where innovation, improved customer experience, increased operational efficiency and information security are key to a company's future.

Figure 33: Worldwide IT Spending Forecast

($ million)	2019 Spending	2019 Gowth (%)	2020e Spending	2020e Growth (%)	2021e Spending	2021e Growth (%)
Data center systems	210,053	0.6	188,365	-10.3	200,094	6.2
Enterprise Software	476,687	11.7	449,506	-5.7	482,666	7.4
Devices	711,525	-0.3	596,914	-16.1	611,303	2.4
IT services	1,040,263	4.8	969,438	-6.8	1,023,179	5.5
Communications Services	1,372,236	-0.6	1,326,492	-3.3	1,366,419	3.0
Overall IT	3,810,764	**2.3**	3,530,714	**-7.3**	3,683,661	**4.3**

Source: Gartner, MainFirst estimates

Besides the fast evolution of technological advances, new entrants have a significant impact on the competitive pressure of the market. In fact, according to Xerfi, the number of new entrants has increased by 16% since 2010.

Nevertheless, international leaders are still dominating the market. We find international giants such as IBM Corporation (US), Microsoft Corporation (US), SAP (Germany), Dell EMC (US), Google Inc (US), Accenture PLC (Ireland), Adobe Systems (US), Oracle Corporation (US), Hewlett Packard Enterprise (US) and Capgemini (FR). Some of these names are Prodware's partners.

Overview of the French digital market

According to Syntec Numérique and IDC, the French digital market grew by 4.2% in 2019, representing a volume of approximately €8.7bn. The previously outlined 'SMACS' mainly explains this dynamic, with net growth estimated at €435m.

The French market is made up of three segments: Consulting and Services (representing approximately 61% of this market), Software Publishing (24%) and Technology Consulting (15%).

Three main segments of the market

- **Software editing**: 2019 growth accelerated to 6.6%, driven by application software (+6.8%, representing CRM, content management and collaborative) and software tools (+8.1%, representing analytical, data management, development, integration, orchestration and quality tools). It should be noted that over the last five years, the growth of the segment has averaged 4.6% per year. SaaS continues to benefit from strong momentum and represents more than 30% of the editing market. General industry, banking, insurance and finance, and the professional services sectors have particularly contributed to this dynamic.
- **Consulting and services** (the digital companies market): 2019 growth was 3.1%, fuelled by new higher value-added service offers (cloud offers, cybersecurity, offers around AI and machine learning, etc.). The Cloud, which reached a 19.9% market share, is driving the market growth (+19.4%). The banking, insurance, and finance, utilities and professional services sectors have particularly contributed to the dynamic.
- **Technology consulting** (or outsourced R&D): the acceleration of services in the process engineering field; the transformation of industrial customers' business models towards the sale of solutions, and the development of services in the devices field (development, security, device management, data management, etc.), have all been driving forces. The main sectors in demand were aeronautics and energy.

Trends observed in the market during 2020

2020 trends

COVID-19 has slowed momentum in the sector. Whereas Syntec Numérique was expecting an increase of approximately 4% in 2020 (including +6.6% for Software Publishing, +2.9% for Consulting and Services, +4.4% for Technology Consulting), it now forecasts a decline of 6.7% for the sector as a whole in 2020. However, there are signs of gradual improvement, with a resumption of ongoing projects and a recovery in commercial activity for 86% of companies.

SMACS remains the driving force, with estimated growth of 3.2% for 2020 (around €450m), driven by the Cloud, where demand for purchases on the Public Cloud should increase by 8% with the crisis. 24% of companies plan to invest in the Cloud to better utilise their data, and 24% will also migrate their applications for availability reasons.

Software Editing: A decline of 3.6% is expected for 2020, with more than 8 out of 10 companies expecting their business to pick up again as of H2 and 40% of publishers expecting their turnover to grow in 2020. The SaaS model remains particularly dynamic, with 86% of companies expecting either stability or growth in the market in 2020.

Consulting and Services: A 6.2% decline is expected for 2020, but the rebound should be sustained, notably thanks to the development of Cloud offers, which is intensifying, and is forecast to reach 23% of the sector's market share in 2020, representing growth of 9.1%.

Technology Consulting: Due to its exposure to the aeronautics and automotive sector, this sector is expected to be the most impacted, also reflected by the order book, which deteriorated in 83% of cases in H1. Depending on the depth of the impact of COVID-19 on this sector, it is estimated that the recovery will therefore vary from 0 to 6 months for pharmaceuticals, energy or telecoms, from 6 to 12 months for the automotive sector, and more than 12 months for aerospace.

Figure 34: French Digital Market Forecast (%)

	2018 Growth (%)	2019 Growth (%)	2020e Growth (%)
Consulting and Services	3.3	3.1	-6.2
Software editing	5.3	6.6	-3.6
Consulting in technologies	5.5	5.0	na
Total Market	4.1	4.2	-6.7

Source: Syntec Numérique, MainFirst estimates

Model development process and alternative approaches

Model theory

We assume that the company's main revenue drivers are a combination of Services/Licences/Hardware sales, SaaS sales and maintenance contracts. We believe Prodware is well placed to capitalise on growth in the digital transformation market with a solid foundation of strategic partnerships and its know-how in terms of innovation. The ramp-up of SaaS should increasingly give a new boost to the group's growth. As part of its development strategy, the group makes targeted bolt-on acquisitions that are not factored into our estimates.

Data sources

- Company data
- MainFirst estimates
- Eikon Thomson Reuters

Processing steps

Significant investments made in recent years in connection with the group's 2016-21 strategic plan should gradually normalise. The ramp-up of SaaS should also contribute to a reduced cost structure and thus to the increase of Prodware's profitability.

Assumptions

Our model is based on figures excluding IFRS16.

Our DCF is based on a conservative 8.7% WACC and a beta of 2.5x in order to integrate the risks.

High capex, increasing indebtedness in recent years, and a slower than expected conversion of the model towards SaaS have weighed on the stock historically. We acknowledge that investors will want to see actual progress before agreeing to pay a full price for the shares, and hence we apply a 20% discount to our valuation methods to reflect these issues, which we may reassess depending on the group's progress.

Limitations

The environment is characterised by a high intensity of competition and an ever-changing landscape with the emergence of new operators.

The group could be impacted by a lack of visibility due to the coronavirus pandemic (cancellation or postponement of projects, risk of default and certain late payments).

In the current economic context, management flexibility in terms of investment and inorganic growth is limited given the current net debt position.

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Prodware (ALPRO FP) as of October 20, 2020 (in EUR)

*Represents the value(s) that changed.
Buy=B; Hold=H; Sell=S; Discontinued=D; Suspended=SU; Discontinued=D; Initiation=I

For a price chart with our ratings and any applicable target price changes for ALPRO FP go to
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