Nice surprise on profitability

Buy

PT: €11.50 (vs €10.00)

Changes	2021E	2022E
Revenue	-5.0%	-5.0%
EPS	4.6%	9.5%

Key data

Ticker	**ALPRO FP**
Price (5 March 2021)	**€6.42**
Upside to Price Target (%)	79.1
Market Cap (m)	50
Free Float (%)	51.9
Daily Value Traded (m)	0.1
Next Reporting Date	May 19 2021
No. of Shares (m)	7.75
1mth perf (%)	12.6
3mth perf (%)	10.3
12mth perf (%)	1.9
12mth high-low (€)	7 - 4

Key financials

(In EUR M)

Year to Dec	2020A	2021E	2022E
Group revenue	172	177	184
EBITDA (rep.)	49.1	50.3	52.5
EBIT (rep.)	19	20.3	22.0
EPS (adj.) (c)	1.51	1.82	1.96
DPS (c)	0.03	0.05	0.06
Net debt/(cash)	112.3	105.0	93.7
ROCE (NOPAT) (%)	7.0	8.3	8.9
EPS (adj.) y/y (%)	6.6	20.8	7.4
Net debt/EBITDA	2.24	2.05	1.75
EV/Sales	1.0	0.9	0.8
EV/EBITDA (adj.)	3.4	3.1	2.8
EV/EBIT (adj.)	8.9	7.9	6.8
P/E (adj.)	4.26	3.53	3.28
Dividend yield (%)	0.5	0.7	0.9
Free CF yield (%)	7.0	25.0	32.9
EV/CE	0.6	0.7	0.6

Prices are as of close 5 March 2021

Completed: 8 March 2021 01:00EST
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All sources unless otherwise stated: Company data, FactSet, Stifel estimates

Share price performance (indexed)

Summary

- The satisfying handling of cost structure resulted in a significant increase in profitability (+200bps vs 2019), allowing the return to a positive FCF
- The ramp-up of SaaS and the roll-out of its proprietary ERP system should contribute to further improvements in profitability
- We upgrade our PT to €11.5 given higher normative EBIT margin and higher trading multiples

Key Points

Nice surprise on profitability. Given the exceptional nature of 2020, revenue declined by 5.6% (€172.4m, lfl), reflecting a resilient activity. SaaS revenue continued to grow (€45m, +15.6%) and represents 26.1% of total revenue. In a context where the COVID-19 crisis has accelerated digital adoption, SaaS subscription models and collaboration tools have proven to be especially well adapted to enabling remote work. The highlight of this annual publication comes from the improvement in profitability (11.1% EBIT margin; i.e. +120bps vs Stifel estimates and +200bps Y/Y) thanks to a satisfying handling of external charges (-22.4%) and staff expenses (-14.2%). During its conference call, the CFO has indicated that some of these savings should continue into 2021. Thus, the ramp-up of SaaS and the roll-out of its proprietary ERP system should improve the profitability and propel the FCF.

Promising signs for 2021 with strong business performance in Q4 2020. Business started picking up right at the beginning of Q3 2020 with new customer wins. With a growing need for digitalisation, especially with regard to support functions, brought on by the generalisation of remote work and e-commerce and the search for efficiency, Prodware relies on its prestigious technological partnerships (Microsoft Dynamics 365, Sage) and its capacity for innovation to offer solutions adapted to all its clients.

Our investment case is still based around three key pillars

- **Acceleration of growth driven by digital transformation.** After the exceptional nature of the year 2020, we are confident in Prodware's ability to deliver an organic growth of 4% in 2022e.
- **Higher margins as company shifts to a SaaS model with the roll-out of its proprietary ERP system.** 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 a catalyst. However, given the current lack of visibility, we conservatively model a 100bps increase in EBIT margins to settle at 12% (normative level vs 10.5% previously).
- **FCF acceleration due to falling capex.** In addition to improving the operating margin, the return to a more normative level of investment (which we identify at around €20m) is forecasted to drive cash flow to €12.4m in 2021e (vs €3.5m in 2020). This improvement will help to alleviate Prodware's high level of net debt, which is a key area of investor concern regarding. It stood at €85.2m in 2020 (ex. IFRS16), or 2.2x EBITDA, limiting the management's financial flexibility.

We upgrade our target price from €10 to €11.5 and keep our Buy rating unchanged. Based on our new estimates (increase in our normative EBIT margin to 12%) and higher trading multiples, we reassess our PT from €10 to €11.5. We continue to apply a 20% discount to our valuation methods to reflect the high levels of capex and increasing indebtedness in recent years, coupled with a small market capitalization and low liquidity. Assuming Prodware delivers on its operational trends and based on our financial estimates, we could see a re-rating of the stock, which currently trades at low EV/EBITDA 21e multiples of 3.2x (ex. IFRS16).

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KEY FINANCIALS AND RATIOS

YEAR TO DECEMBER (IN EUR m)	2019A	2020A	2021E	2022E
PROFIT & LOSS ACCOUNT				
Group revenue	**188**	**172**	**177**	**184**
EBITDA (rep.)	**46.5**	**49.1**	**50.3**	**52.5**
EBIT (rep.)	**17.29**	**19**	**20.3**	**22.0**
Pre-tax results	10.9	13.1	15.7	17.3
Income tax and other items	(0)	(2)	(2)	(3)
Net result group	10.4	11.4	13.4	14.4
Minorities and other items	0.11	(0)	(0)	(0)
Net result shareholders, rep.	**10.5**	**11.2**	**13.2**	**14.2**
EPS, fully diluted (c)	**1.01**	**1.07**	**1.30**	**1.39**
Exceptionals in EBIT	0.01	0.30	0	0
Profit and Loss Account (adj)				
EBITDA	**48.3**	**50.1**	**51.3**	**53.5**
EBIT	**17.28**	**18.90**	**20.3**	**22.0**
Operating result (company definition)	17.3	19.2	20.3	22.0
Net result, shareholders	10.5	11.3	13.6	14.6
EPS (adj.) (c)	**1.41**	**1.51**	**1.82**	**1.96**
CASH FLOW STATEMENT				
EBITDA (rep.)	46.5	49.1	50.3	52.5
Cash interest and tax payments	5.74	6.00	5.81	6.48
Change in working capital	3.27	(9)	0.46	0.23
Other operating cash flow items	(22)	(20)	(18)	(19)
Cash flow before capex	**33.7**	**26.1**	**38.4**	**40.4**
Capital expenditure	(37)	(23)	(26)	(24)
Free cash flow	**(3)**	**3.50**	**12.4**	**16.4**
Acquisitions/Disposals/Financial assets	0.11	0	0	0
Dividends, minority payouts	(0)	0	0	0
Equity measures, other	(33)	(3)	(5)	(5)
Change in net cash	(36)	0.46	7.32	11.3
Net cash (debt)	**(113)**	**(112)**	**(105)**	**(94)**
BALANCE SHEET				
Fixed assets	214	218	218	218
Goodwill	34.6	32.6	32.6	32.6
Current Assets	146	163	146	160
t/o Inventories	0.06	0.10	0.10	0.10
t/o Trade receivables	53.2	74.2	50.8	52.8
t/a Cash and equivalents	3.81	10.5	17.8	29.1
Group equity	145	155	172	188
t/o Shareholders equity	144	155	172	188
Interest-bearing liabilities	117	123	123	123
Other liabilties and provisions	98.4	102	69.7	67.1
t/ Pension provisions	5.70	5.90	5.90	5.90
t/o Trade libabilities	23.6	19.7	24.6	21.9
Balance sheet total	**360**	**380**	**364**	**377**
Net Working Capital	29.7	54.6	26.3	31.0
Capital Employed (incl. Goodwill)	243	272	244	249
RATIOS				
Revenue y/y (%)	6.7	(8.2)	2.5	4.0
EBITDA Margin (adj.) (%)	25.8	29.1	29.1	29.1
EBIT adj margin (%)	9.2	11.0	11.5	12.0
EPS (adj.) y/y (%)	18.6	6.6	20.8	7.4
Working capital intensity (%)	15.8	31.7	14.9	16.9
DSOs	104	157	105	105
Inventory turnover (Days)	0.11	0.21	0.21	0.20
Net debt (cash) / EBITDA (adj.)	2.33	2.24	2.05	1.75
EBITDA (adj.) / Capex	1.30	2.22	1.97	2.23
Free CF yield (%)	(6.7)	7.0	25.0	32.9
Oper. FCF Yield (%)	(5.4)	(1.5)	4.1	6.6

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 40% in 2022) should contribute to a reduced cost structure and therefore increase Prodware's profitability to 12% from 9.1% 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 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 9.4% 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 current economic context (cancellation or postponement of projects)
- More competitive pressure, especially in attracting the best employees
- Limited financial manoeuvres in the current economic context

Key dates

- Q1-21 Sales release: 19 May 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: 2.7%
- Employees: 1.0%
- Treasury shares: 5.3%

Senior management

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

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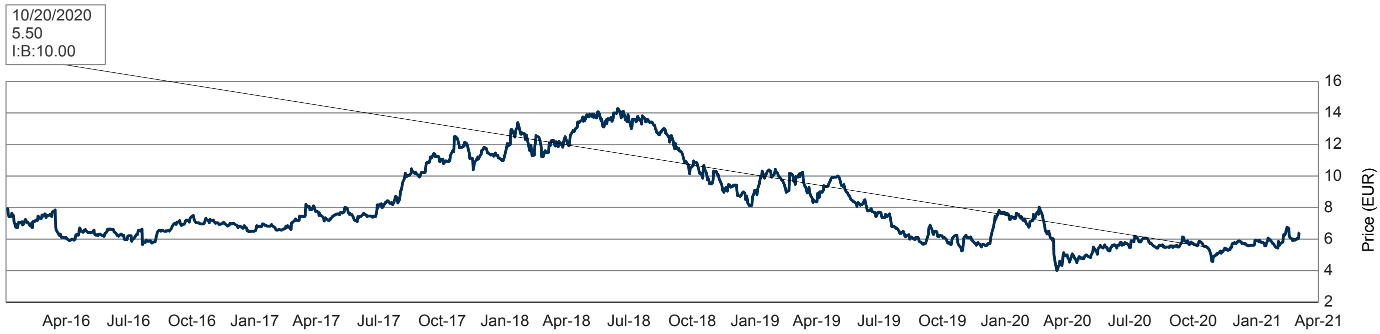
Prodware (ALPRO FP) as of March 05, 2021 (in EUR)



*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 http://stifel2.bluematrix.com/sellside/Disclosures.action?ticker=ALPRO FP

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[1] This rating is only utilised by Stifel Canada.

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