

## DATAGROUP

**IT services**
**26 February 2018**

### Acquisitions significantly broaden the offering

FY17 was a year of strong growth for DATAGROUP, with revenues rising by 28% and EBITDA surging 42%. The EBITDA margin rose by 120bp to a record 12.1%. The core cloud services continue to grow strongly, rising by 64% and recurring sales represented 70% of total revenue (which translated to 88% of gross profit), up from 66% in FY16. In August 2017, DATAGROUP acquired ikb Data to extend the group's offering into the financial services sector and in January 2018 it announced the acquisition of Almato, a pioneer in Robotic Process Automation. Consequently, DATAGROUP is building a number of key differentiators in its markets.

### Consolidating a fragmented IT services market

DATAGROUP is consolidating the highly fragmented German IT services market, focusing on Mittelstand companies with €100m-€1bn revenues. This involves both buy-and-build and buy-and-turnaround approaches, transitioning the acquired businesses to DATAGROUP's more effective business model. DATAGROUP's CORBOX solutions are cloud-based, focused on fixed-price contracts, based on standardised processes that are certified according to ISO 20000 and backed by service level agreements (SLAs). DATAGROUP believes there is a huge opportunity in the Mittelstand space, as these companies typically rely on their own expensive in-house IT departments and have difficulty adapting to new technologies. The broad range of services allows customers to fully outsource their IT operations. Much of the work is done remotely, and the group can scale its data centre services and shared services desk to support a large number of customers.

### FY17 results: Surprise dividend increase

FY revenue grew by 28% to €223m, while EBITDA surged by 42% to €27m. As a result of strong operating cash flow of €32.5m and the €21.1m capital increase, net debt tumbled by €20.3m to €10.6m. The company is recommending a 50% hike in the dividend to 45c. Following the results, DATAGROUP announced the acquisition of Almato for an undisclosed price. Almato is a fast growing and profitable business operating in the productivity enhancing Robotic Process Automation (RPA) space.

### Valuation: Premium reflects strong business drivers

While the shares are trading on more expensive metrics than historically, at 1.3x consensus FY19e sales and 11x EBITDA, the outlook remains underpinned by attractive business drivers, which provides a compelling case for acquisitions.

#### Consensus estimates

Year end	Revenue (€m)	EBITDA (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
09/16	174.9	19.1	0.75	0.30	58.7	0.7
09/17	223.1	27.0	1.41	0.45	31.2	1.0
09/18e	270.0	31.8	1.73	0.48	25.6	1.1
09/19e	286.0	34.1	2.09	0.55	21.2	1.2

Source: Bloomberg

**Price** €44.05  
**Market cap** €368m

#### Share price graph



#### Share details

Code D6H  
 Listing Deutsche Börse Scale  
 Shares in issue 8.349m  
 Last reported net debt at 30 September 2017 €10.6m

#### Business description

DATAGROUP is a full IT outsourcing provider, focused on the German Mittelstand market. The company offers the full range of IT services on a modular basis, through its CORBOX "cloud-enabling platform". Services include service desk, end-user services, data centre services, application management and SAP services.

#### Bull

- A compelling growth strategy, scaling the business across the Mittelstand sector.
- Cloud services business model gives it a clear advantage over competitors.
- Centralised SLA-based approach with a focus on customer satisfaction puts company in strong position to consolidate a fragmented market.

#### Bear

- The group's valuation metrics are more expensive than they have been.
- Highly exposed to the German economy.
- Acquisitions bring risks, but DATAGROUP has a proven track record in integrating acquisitions.

#### Analyst

Richard Jeans +44 (0)20 3077 5700

[tech@edisongroup.com](mailto:tech@edisongroup.com)  
[Edison profile page](#)

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## Final results: Cloud services jumped by 64% to €125m

Group revenue rose by 27.6% to €223.1m as EBITDA lifted by 41.6% to €27.0m, for a 120bp increase in the margin. The growth included a first full-year contribution from the HPE acquisition (consolidated from late FY16) and an initial contribution from HanseCom (consolidated from May 2017). Excluding the effect of acquisitions, we estimate organic growth was c 3%.

The company has continued to shift its time and materials (T&M) customers to its modular CORBOX fixed-price cloud platform. As T&M are lower-margin revenues, this enables the group to expand its profit margins. Revenues from cloud services jumped by 64% to €125m, while revenue from non-cloud services fell by 18% to €32m, reflecting the ongoing transition. Other services, which include implementation projects as well as some proprietary software, rose by 14% to €24m. Net income almost doubled to €11.2m while EPS jumped by 88% to €1.41.

18 new CORBOX customers were added during the year, which was slightly below the 20 targeted. However, the average annual revenue run rate was slightly above the €750k the group targets. There were also eight significant upsells. Churn remains very low as the company rarely loses clients. Labour costs are tight in the key metropolitan areas, eg Stuttgart, Hamburg, Dusseldorf.

End September net debt of €10.6m, down from €31m at end September 2016, was boosted by the April 2017 c €21m capital increase. Consequently, the end-FY17 equity ratio was 27.9%, comfortably above the targeted minimum of 20%. Capex jumped from €1.8m in FY16 to €8.5m in FY17, as the group had to provide desks and computers for its new employees, including those who joined from HPE. Additionally, the group moved to new offices in Hamburg and Cologne. No financial guidance has yet been given. Guidance for FY18 will be given at the time of the AGM on 8 March. Q1 results will be published on 28 February.

The Management Board and the Supervisory Board will propose to the AGM that the dividend be raised again this year to 45c per share.

### Exhibit 1: Financial summary

€000s	FY12	FY13	FY14	FY15	FY16	FY17
	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
<b>Income statement</b>						
<b>Revenue</b>	<b>146,183</b>	<b>156,935</b>	<b>152,380</b>	<b>157,574</b>	<b>174,918</b>	<b>223,142</b>
Services & maintenance revenue	102,980	116,082	114,413	120,773	135,907	180,631
% group revenue	70%	74%	75%	77%	78%	81%
Trade revenue	42,923	40,541	37,707	36,592	38,821	42,297
Other/consolidation	280	312	260	209	190	214
<b>EBITDA</b>	<b>9,549</b>	<b>12,553</b>	<b>11,686</b>	<b>15,339</b>	<b>19,103</b>	<b>27,041</b>
EBITDA margin	6.5%	8.0%	7.7%	9.7%	10.9%	12.1%
EBIT	3,792	6,091	6,213	9,604	12,675	18,590
EPS	0.37	0.25	0.14	0.65	0.75	1.41
DPS	0.20	0.20	0.20	0.25	0.30	0.45
<b>Balance sheet</b>						
Total non-current assets	69,647	66,109	60,754	68,062	92,178	102,864
Total current assets	31,019	35,590	34,345	35,285	67,568	110,526
<b>Total assets</b>	<b>100,666</b>	<b>101,699</b>	<b>95,099</b>	<b>103,346</b>	<b>159,746</b>	<b>213,390</b>
Total non-current liabilities	(32,416)	(49,420)	(44,056)	(39,013)	(97,367)	(95,881)
Total current liabilities	(45,552)	(29,767)	(29,778)	(40,283)	(34,012)	(57,928)
Total liabilities	(77,968)	(79,188)	(73,834)	(79,296)	(131,379)	(153,809)
<b>Net Assets</b>	<b>22,698</b>	<b>22,511</b>	<b>21,264</b>	<b>24,051</b>	<b>28,367</b>	<b>59,581</b>
<b>Cash flow</b>						
Net cash from operating activities	8,456	10,947	9,286	9,431	9,518	32,477
Net cash from investing activities	(17,950)	(5,210)	(4,301)	(9,295)	(3,711)	(19,749)
Net Cash from financing activities	12,056	2,778	(6,937)	(7,513)	16,545	16,027
<b>Net Cash Flow</b>	<b>2,562</b>	<b>8,516</b>	<b>(1,951)</b>	<b>(7,375)</b>	<b>22,352</b>	<b>28,755</b>
<b>Cash &amp; cash equivalent end of year</b>	<b>2,883</b>	<b>11,398</b>	<b>9,448</b>	<b>2,072</b>	<b>24,424</b>	<b>53,179</b>

Source: Company accounts

## Outlook and strategy; shift to the cloud is proceeding well

DATAGROUP is focused on delivering cloud solutions to Mittelstand companies. The group has chosen to focus entirely on Germany, given that the market is so large (BITKOM – IT services €38bn) and DATAGROUP estimates that the Mittelstand sector alone is worth c €20bn, while CORBOX revenues are just c €80m.

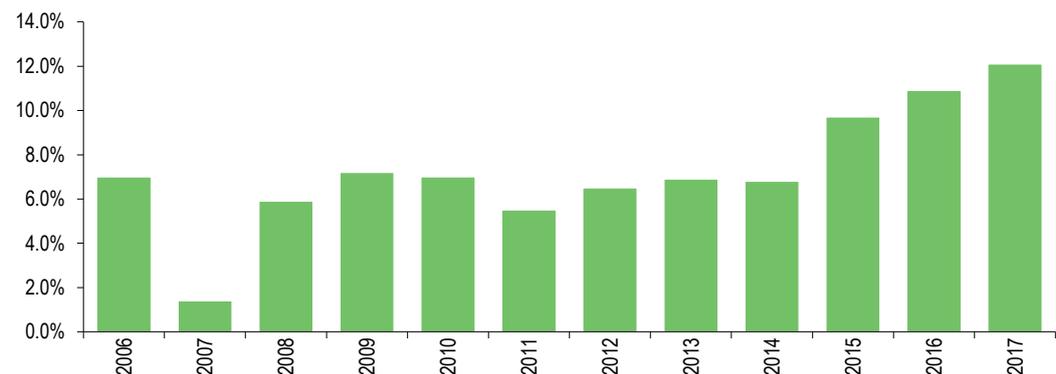
The group's strategy has involved improving the quality of revenues, by shifting to recurring cloud-based revenues on higher-margin, fixed-term contracts from the traditional T&M-based work. By offering a centralised and standardised SLA-based approach, the group has been able to establish a significant advantage over smaller competitors. Further, its strong focus on customer satisfaction gives it an advantage over larger players, which tend to focus their efforts on their bigger global customers.

Management's goal remains for DATAGROUP to generate €500m revenues by FY21. This includes c 11.7% of annualised organic growth and c €150m of revenue from acquisitions. A prime objective is to lift EBITDA margins to 13% by FY20/21 (12.1% in FY17). Growth will also come from upselling to existing customers.

The group's impressive organic revenue growth has been in spite of the following:

1. As DATAGROUP makes new acquisitions it eliminates unprofitable activities.
2. The planned decline in guaranteed revenues from the HPE transaction (which was announced in July 2016).

### Exhibit 2: EBITDA margins have been rising strongly



Source: DATAGROUP

### 3. Acquisition strategy

DATAGROUP has been highly active in the German IT services sector's consolidation process, acquiring inefficiently run businesses as well as strategic assets, and it has made 21 acquisitions since its IPO in September 2006. Merger drivers include benefits from the centralised support, virtually centralised Service Desk, along with economies of scale from accounting, HR, management, marketing and scaling data centre assets. The key components in the strategy are:

- good technology, such as the recent robotics automation acquisition of Almato;
- adding customers; and
- adding skills, particularly SAP, IoT and big data related.

The company has a strong track record of integrating acquisitions. Additionally, the group retains a healthy balance sheet, following the capital raising in April last year.

## Recent acquisitions

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DATAGROUP has made two acquisitions over recent months, taking the total number of acquisitions since the IPO in 2006 to 21. These two deals add to the solution set and provide the opportunity for cross-selling. The group has a pipeline of further potential deals.

### Acquisition of ikb Data

In August 2017, DATAGROUP acquired ikb Data from IKB Deutsche Industriebank (IKB) for an undisclosed sum. IKB has been selling non-core assets to simplify its corporate structure. At the time the deal was announced, ikb Data had 73 employees and generated revenues of more than €27m in the year to March 2017.

There are two key reasons for the acquisition:

1. ikb Data has a highly attractive customer base, including IKB itself, which generates c 60% of revenue. IKB will become one of the group's largest customers generating revenues of c €16m. IKB has a long-term contract with ikb Data, but clearly there are risks that the contract could be ended, especially if IKB is sold. The balance of ikb Data's customers comprises mainly financial services firms.
2. The acquisition satisfies DATAGROUP's objective to establish a solution set for the banking sector. Given the stringent regulations in the financial services industry, this would have been very difficult for DATAGROUP to have achieved on its own.

The initial revenues from the acquisition are expected to be lower than the €27m achieved in FY17 due to DATAGROUP's policy of cutting out loss-making contracts when it acquires businesses. However, the group will benefit from synergies and, given ikb Data's strong financial services industry know-how, DATAGROUP expects additional growth potential. ikb Data's special expertise is documented by many relevant certificates, eg ISO 20000 and ISO 27001 as well as ISAE 3402.

### Acquisition of Almato

On 29 January, DATAGROUP announced the acquisition of Reutlingen-based robotic specialist Almato. Almato broadens DATAGROUP's CORBOX portfolio by enabling customers to automate their digital business processes. DATAGROUP made the acquisition as it believes that automation will be critical to ensure the future competitiveness of service companies. DATAGROUP also intends to use Almato's technology to automate some of its own processes.

Founded in 2002, Almato is a provider of software for optimising standard business processes. The company uses a value-added reseller network in Germany, which we understand DATAGROUP plans to retain. Almato offers RPA and Real-Time Interaction Management (RTIM) for both full and partial automation. Its customers operate across a range of industries including telecommunications, utilities, finance, retail, general industrials and tourism, and include both German domestic and international companies. Almato's customers typically rate service quality and customer satisfaction as key differentiators. Almato has 40 employees and generated annual revenue of c €4m in 2016 with a double-digit EBITDA margin. The acquisition price was not disclosed and Almato is expected to be consolidated into the group accounts from March 2018.

## Recent newsflow

### State of Hesse launched BAföGdirekt app

In January, the State of Hesse launched its new BAföGdirekt app, developed by DATAGROUP. This software development activity is reflected in DATAGROUP's 'Other services' segment.

BAföGdirekt enables the paperless processing of applications for BAföG (Federal Training Assistance Act) or AFBG (Ascended BAföG). Documents such as account statements and tax assessments can be photographed with smartphones and tablets and transmitted directly to the office via a secure connection. This simplifies the communication between the applicant and the funding office by eliminating the need for cumbersome scanning and uploading of the requisite forms. Further, BAföGdirekt can notify the user about any change of the application status. 40% of all BAföG applications are currently processed with the BAFSYS (BAföG and AFBG system) specialist procedure developed by DATAGROUP in nine federal states. While State of Hesse is the first state to offer BAföGdirekt, other German states are also planning to use the app.

### 2017 German IT Outsourcing Survey results January 2018

In the latest survey on customer satisfaction by Whitelane Research and Navisco, DATAGROUP retained its second place position, with a slightly improved score of 80%. This compares with the average score of 68%. DATAGROUP achieved first place in the categories of account management and transformation quality with 83% and 78% respectively, while attaining high scores in the categories of quality of service provision, flexibility and proactivity. Strong customer focus is a key component in the group's strategy.

## Valuation

DATAGROUP's shares have had an impressive run, rising from €2 in 2009 to reach €47 in January. Nevertheless, the business is still small, with a market capitalisation of c €370m, while the target market is a growth market and huge. The acquisition of Almato adds a new dimension to the investment case. We note that Blue Prism, a UK-based peer, listed on the UK AIM market in March 2016, after pricing its IPO at 78p, and is now priced at 1,578p. Blue Prism is trading at c 23x FY18e sales and is not forecast to record a profit for years.

### Peer valuation

The shares trade at a discount to its broad peer group in terms of P/E. This is in spite of the favourable growth prospects, healthy recurring revenues (70% of group revenues) and strong business drivers.

**Exhibit 3: Peer group comparison**

	Share price	Market cap	EV/sales (x)		EV/EBITDA (x)		PE (x)	
	local curr		(€ m)	Year 1	Year 2	Year 1	Year 2	Year 1
<b>DATAGROUP</b>	<b>44.05</b>	<b>368</b>	<b>1.40</b>	<b>1.32</b>	<b>11.9</b>	<b>11.1</b>	<b>25.6</b>	<b>21.2</b>
Allgeier	26.3	262	0.65	0.57	12.5	9.3	47.7	24.4
ATOS	114	12,021	0.96	0.94	7.2	6.7	12.8	11.8
Bechtle	71.15	2,988	0.84	0.76	15.2	13.4	25.6	22.3
Cancom	78.25	1,371	1.16	1.07	15.7	13.3	31.7	26.5
CENIT	21.8	182	1.05	0.91	12.1	9.4	24.0	18.8
GFT	13.2	348	1.05	1.01	11.3	10.0	18.0	15.2
QSC	1.386	172	0.71	0.72	6.5	6.4	69.30	27.7
Realtech	1.43	8	N/A	N/A	N/A	N/A	N/A	N/A
S&T	20.76	1,317	1.61	1.43	22.6	17.4	43.1	29.0
SNP Schneider	35	192	1.64	1.32	57.0	16.0	1398.0	38.5
USU Software	25.8	272	2.99	2.67	64.9	32.1	42.0	25.1
All for One Steeb	70.6	352	1.05	0.96	10.7	9.4	23.1	19.7
<b>Medians excluding DATAGROUP</b>			<b>1.05</b>	<b>0.96</b>	<b>12.5</b>	<b>10.0</b>	<b>31.7</b>	<b>24.4</b>

Source: Bloomberg. Note: Prices as at 22 February 2018.

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