

20th January 2016

TMT

## Software AG

Price EUR28.96

Feedback from FY15 results conference call: momentum improving, better confidence ahead

Fair Value EUR34 vs. EUR33 (+17%)

BUY

Bloomberg	SOW GR
Reuters	SOWG.DE
12-month High / Low (EUR)	29.0 / 22.1
Market Cap (EURm)	2,287
Ev (BG Estimates) (EURm)	2,229
Avg. 6m daily volume (000)	216.1
3y EPS CAGR	9.7%

We are reiterating our Buy rating and have increased our DCF-derived Fair Value to EUR34 from EUR33 as we have raised our adj. EPS ests. by 4% for 2015 and 3% for 2016-18. The solid FY15 results pre-announced yesterday in our view show that the efforts made to improve 'go-to-market' and sales productivity are now bearing fruit. Revenue momentum is improving, and non-IFRS op. margin is well on the way to reach 32-35% by 2020. While lfl revenue growth was still negative in 2015 (est. -1.7%), we are convinced Software AG will be able to post a positive level in 2016 (est. +2.9%), provided that no economic shock happens.

	1 M	3 M	6 M	31/12/15
Absolute perf.	11.9%	18.5%	14.1%	9.6%
Softw. & Comp.	-3.5%	4.9%	0.0%	-4.7%
DJ Stoxx 600	-7.8%	-8.6%	-17.9%	-9.0%

### ANALYSIS

- Digital Business Platform (DBP):** efforts bearing fruit quarter after quarter. The strong DBP growth in Q4 (sales +11% lfl, o/w +17% lfl on licence sales) stemmed from an outstanding performance in the US and in EMEA (licences +18% in the US, x3 in the UK, +72% in France, +22% in Middle East, +66% in Nordic countries, +62% in Eastern Europe) despite a poor quarter in Brazil and uncertainties in Asia Pacific. The number of large deals above EUR1m increased by 37% in 2015, the average deal size was up 13% in 2015 (+36% in Q4), and DBP sales productivity surged by 40% at cc in Q4 and above 20% at cc for the full-year. The number of active indirect sales partners surged by 60% in 2015. DBP cloud bookings were up 66% in Q4 (+131% for FY15). Software AG is reaping the benefits of the sales transformation it underwent a year ago under the management of Eric Duffaut, with a lot of work done on the value proposition sold to clients and a couple of large digital transformation deals won recently (Bosch, EDF, Wells Fargo, Boots Alliance...).
- A&N (Adabas & Natural) to be there beyond 2015, Consulting transformation achieved.** The resilience of A&N revenues is no longer surprising as Software AG has a lot of focus on customer retention, and clients are not left behind: they have been offered premium support and they are accompanied in their digital transformation. Management is confident A&N will deliver for 2016 a business line margin close to the 70% reported for 2015. Finally, Consulting has achieved its transformation, with 40 new customer references in 2015 and a move away from the project-based model which looks to augur a sustainable double-digit business line margin in our view.
- Confidence in 2020 targets.** The business line margin was up for all divisions in 2015: +2.5ppt to 29% for DBP, +1.8ppt to 70% for A&N, +3.5ppt to 11.3% for Consulting), not by cutting costs per se, but by optimising sales productivity (on DBP, indirect sales excl. US Federal are close to 15% of revenues while they were below 10% one year ago) and the product and service portfolios, and better selectivity in terms of geographies. FY16 company guidance (DBP product sales up 5-10% at cc, A&N product sales down 4-8% at cc, non-IFRS operating margin of 30-31%) brings more confidence to be on track for achieving the 32-35% target set a year ago for 2020 - provided that an economic shock does not jeopardise it. For 2016, thanks to the improving trend in the DBP division we expect 2.9% lfl revenue growth – the first year of positive lfl growth since 2010.

YEnd Dec. (€m)	2014	2015e	2016e	2017e
Sales	857.8	873.2	892.1	925.2
% change		1.8%	2.2%	3.7%
EBITDA	250	278	290	309
EBIT	238.0	264.4	275.6	294.4
% change		11.1%	4.2%	6.8%
Net income	164.5	184.2	193.3	207.7
% change		12.0%	5.0%	7.4%

	2014	2015e	2016e	2017e
Operating margin	27.7	30.3	30.9	31.8
Net margin	12.9	15.6	17.3	18.3
ROE	10.9	13.0	13.4	13.2
ROCE	16.6	19.8	20.7	22.7
Gearing	7.0	-5.6	-17.3	-27.5

(€)	2014	2015e	2016e	2017e
EPS	1.86	2.28	2.28	2.45
% change	-	23.0%	-0.2%	7.4%
P/E	15.6x	12.7x	12.7x	11.8x
FCF yield (%)	5.3%	8.1%	7.9%	8.4%
Dividends (€)	0.50	0.55	0.60	0.65
Div yield (%)	1.7%	1.9%	2.1%	2.2%
EV/Sales	2.7x	2.6x	2.3x	2.1x
EV/EBITDA	9.4x	8.0x	7.2x	6.3x
EV/EBIT	9.9x	8.4x	7.6x	6.6x



### VALUATION

- Software AG's shares are trading at est. 7.6x 2016 and 6.6x 2017 EV/EBIT multiples.
- Net debt on 30th September 2015 was EUR1.7m (net gearing: 0%).

### NEXT CATALYSTS

- Final FY15 results** on 27th January before markets open.
- Investor Day** on 10th February in Darmstadt (Germany).

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