

Sector View

TMT

Q4 2015 review, and our TMT Top Picks for Q1 2016: Atos, Wirecard and Worldline

	1 M	3 M	6 M	31/12/14
Softw. & Comp.	-2.1%	14.5%	9.1%	25.0%
DJ Stoxx 600	-6.5%	-0.2%	-7.4%	4.3%

*Stoxx Sector Indices

Companies covered

Company	Rating	Fair Value
ALTEN	NEUTRAL	EUR48 vs. 44
ALTRAN TECHNOLOGIES	BUY	EUR13
ARM HOLDINGS	BUY	1310p
ASML	NEUTRAL	EUR76
ATOS	BUY	EUR93 vs. 94
AXWAY SOFTWARE	BUY	EUR30
CAPGEMINI	BUY	EUR96
CAST	BUY	EUR4.4 vs. 4.7
DASSAULT SYSTEMES	SELL	EUR65 vs. 66
DIALOG SEMICONDUCTOR	NEUTRAL	EUR37
GAMELOFT	BUY	EUR6.7
GEMALTO	NEUTRAL	EUR69
INDRA SISTEMAS	SELL	EUR10 vs. 9.8
INFINEON	BUY	EUR15
INGENICO GROUP	BUY	EUR150
SAGE GROUP	NEUTRAL	550p vs. 540
SAP	NEUTRAL	EUR75
SOFTWARE AG	BUY	EUR33
SOITEC	NEUTRAL	EUR0.8
SOPRA STERIA GROUP	BUY	EUR115
STMICROELECTRONICS	SELL	EUR6.8
SWORD GROUP	BUY	EUR28
TEMENOS GROUP	BUY	CHF52 vs. 47
UBISOFT	BUY	EUR37
WIRECARD	BUY	EUR52
WORLDLINE	BUY	EUR29

LOOKING BACK ON Q4 2015

In Q4 2015, the performance of the Technology sector was outstanding. Over the period, the DJ STOXX Europe Technology index surged by 19% and outperformed the DJ STOXX Europe 600 index by 13ppt (+6%), on the back of the stockmarket catch-up in October after last summer's concerns regarding the Chinese economy vanished. In addition, we cannot rule out that during the same month the anticipation of an extension of the ECB's 'quantitative easing' policy until March 2017 did help.

During the period, the best performers were Gameloft and Ubisoft (respectively +84% and +47%, Vivendi's entry in their share capitals and then speculation), Infineon (+34%, great integration of International Rectifier leading to market share gain and margin improvement) and Temenos Group (+30%, Q3 15 results above expectations). The worst performers were Dialog Semiconductor (-13%, rumours of fragile iPhone supply chain, downward revision of the Q4 guidance, and the controversial acquisition of Atmel), Cast (-7%, 'soft' quarter in Q3 15), Indra Sistemas (-7%, further write-offs in Brazil and mounting worries on LatAm) and Gemalto (-5%, lower sales to mobile operators). Our sector Top picks Wirecard and Ingenico Group, were up respectively 9% and 8%.

NEW ESTIMATES AND FAIR VALUES

We take the opportunity to update our forecasts for 2015-2018 and DCF-derived fair values: 1). The roll-over of our models to 2016 for the companies under coverage for which we haven't yet done (Alten, Axway, Cast, Indra, Sopra Steria, and Temenos); 2). Update in our forward fx assumptions (slightly positive for Sage, slightly negative for Dassault Systèmes, Atos, Indra and Sopra Steria); 3). Marginal company-specific changes to our models (more caution on LatAm for Indra due to the economic environment in Brazil); 4). The specific case of Temenos, which trades in CHF but reports in USD while the CHF/USD rate fell by 5% since our last update on the stock (21/10/15).

As such, we adjust our DCF-derived fair value on Alten (EUR48 vs. EUR44), Atos (EUR93 vs. EUR94), Cast (EUR4.4 vs. EUR4.7), Dassault Systèmes (EUR65 vs. EUR66), Indra Sistemas (EUR10 vs. EUR9.8), Sage Group (550p vs. 540p) and Temenos Group (CHF52 vs. CHF47).

WHAT WE SEE FOR Q1 2016

For Software & IT Services, based on industry analysts' forecasts, we anticipate stable growth or a slight slowdown in global IT spending for 2016, with est. +5-6% for Software (vs. +6% in 2015) - still driven by the now established SaaS model - and an est. +3-4% for IT Services (vs. +4%) - driven by transformation projects in Application Services and IT Consulting while Infrastructure Services are likely to be flat due to the ramp-up of cost-efficient clouds. The main drivers of the market continue to be digital transformation (cloud, mobile, analytics/big data, social networks, security) and a moderately positive but increasingly volatile economic environment (stable growth in North America, modest improvement in Europe, volatility in emerging countries). In High-tech Consulting, the market is expected to maintain modest recovery thanks to better visibility in Aerospace & Defence.

In Payments, companies should continue to benefit fully from the EMV migration in the US (in the US, 60% of the 13m POS devices, i.e. 8m, still need the EMV upgrade according to VeriFone), the equipping of emerging markets (notably the growing installed base of terminal POS in China which should double from 2014 to 2017), the management of the installed base in mature countries, the growing importance and good performance expected from e-commerce during the festive season, and the rising demand for security in electronic payments. 1/ Ingenico Group (Buy – FV of EUR150; 100% of its sales in payment) has the best commercial offer in multi-channel payment and we are still confident for Q4 2015 following VeriFone's comments. The group should post 13.2% organic growth in FY15 (i.e. +8.2%e in Q4; since VeriFone released its Q4, we believe Ingenico is likely to post a performance in a range of +8/+11%) with an EBITDA margin of 23.3% (-10bp Y/Y) vs. management's guidance of +12/13% and ~23% respectively. 2/ Wirecard (Buy – FV of EUR52; pure player in online payments) should post FY15 organic growth of 23.5% (i.e. +22.3%e in Q4) driven by the expanding online payment segment and notably south-east Asia, which should translate into the high-end of its EBITDA guidance range of EUR223-232m (BG. EUR231m, a margin of 30.0% +120bp). 3/ Worldline (Buy – FV of EUR29; ~70% of its 2015 sales in payment). Since the acquisition of Equens, Worldline should now be fully considered as a PSP (#1 in Europe vs. #3 before). It should post a FY15 organic growth of 4.3% (i.e. +4%e in Q4, taking

into account the end of the technical car control contract in the UK which is already known from its IPO) with an EBITDA of EUR19.2% (+50bp Y/Y) vs. Worldline's guidance of +4/5% and +50bp in pro forma terms respectively. **4/ Gemalto** (Neutral – FV of EUR69; ~30% of its sales in payment) should post lfl sales growth of 7.8% in FY15 (i.e. +6.7%e in Q4, impacted by lower sales to mobile operators) with a PFO of EUR421m, i.e. +10% Y/Y (margin of 13.4%, -210bp) vs. a vague guidance of double-digit growth in PFO. We believe there are still too many risks in its SIM and related services businesses.

For Video Games: by taking equity stakes in Ubisoft and Gameloft, Vivendi has encouraged investors to change the way they look at video games shares. On these two particular shares, only speculation (and not financial releases) will drive the share prices in the next few months. We believe Vivendi will launch a public tender offer on **Gameloft** in the short term (hostile or friendly, it will succeed in our view) to force Ubisoft to enter into discussions and convince the Guillemot family that there are synergies between both groups. And finally, we expect a friendly takeover bid on **Ubisoft** sometime in 2016e. It's now time to try to value the entire cycle. Note that our FVs on Ubisoft (Buy, FV of EUR37) and Gameloft (Buy, FV of EUR6.7) reflect minimum prices in the case of takeover bids.

In Semiconductors, we forecast weak momentum on PC, tablet and smartphone sales representing together about 2/3rds of total semiconductor sales. Q4 2015 has been impacted by a complex environment and temporary inventory adjustments in the automotive and industrial sectors, resulting in low visibility in these sectors which we expect to gradually return to normal in Q1 2016. Overall, we continue to believe that these two segments and the IoT are poised to drive growth in the medium/long term. Regarding semi equipment makers, 2016 should be the year of the 10nm ramp at IDM and foundries which is expected to trigger equipment orders, however, the current market environment could delay the ramp up of the 10nm process technology initially expected to ramp up from Q2 2016.

In Telecoms, after the takeover of SFR by Numericable in late 2014, the French Telecom market entered a new era in 2015, but stabilisation of the market is still a long way ahead. As 2016 begins, Iliad still needs to find a smooth way out of its national 2G/3G roaming agreement with Orange while accelerating the roll-out of its mobile and fibre networks. Numericable-SFR is still in a restructuring phase but has to regain momentum on the commercial side. And Bouygues Telecom needs sustained customer growth in order to make its recovery dreams come true, while Orange is investing billions of euros to maintain its leadership in 4G and catch up with Numericable-SFR on the very high speed fixed side (fibre/cable). But something else is happening backstage: merger talks between Orange and Bouygues Telecom, involving all players and raising major competitive concerns, which could have a disruptive effect on the market. In many other European countries such as the UK, Spain, Belgium or Portugal, the reconfiguration of markets following M&A operations should also be closely monitored.

CONCLUSIONS AND TOP PICKS

In Software & IT Services, while we deem the current mixed economic news-flow will not urge investors to invest pure "growth" stories, we recommend to buy specific earnings-enhancing stories based on M&A. As such, we reintroduce Atos in our Top Pick list. 1). Atos is highly focused on the structurally stable Managed Services/BPO businesses and can only generate low organic growth out to 2018; 2). The project to acquire Unify should help Atos generate an accretive impact on EPS of at least 15% as of 2017, while the Equens takeover project via subsidiary Worldline should enhance EPS by 4-5% as of 2018 in our view; 3). Atos has expanded over the decades via acquisitions and this method is now part of its DNA, and, since the arrival of Thierry Breton at the head of the group, Atos has been faultless in integrating its acquisitions and delivering synergies; 4). Yet the rumours reported by the press since mid-December (*Re/code*, *Economic Times*) are not confirmed, and we estimate Atos may create another EPS enhancing story in case of a bid on Dell's Perot Systems business.

In Payments, we expect investors to show an increasing appetite for the electronic payments and digital security themes by betting on payment service providers (PSP). As such, **we keep Wirecard (Buy, FV EUR52) in our Q1 Top Pick list to benefit from the rising momentum of the eCommerce** (notably during the Christmas period) and a good visibility (first 2016 guidance already given). The group is a growth story (we see our +23.5% as a minimum) and one of margin improvement (we expect +120bp thanks to its fixed-cost structure). We believe it will come in at the high-end of its FY15 EBITDA guidance range and above the consensus (which is at the middle of the guidance range). The share is attractive relative to its EPS growth (2016e: P/E of 25x vs. +38% attrib. net profit). **We also include Worldline (Buy, FV EUR29) in our list** because, since the acquisition of Equens, it will become the #1

PSP in Europe (77% of its pro forma sales will be derived from payment). Worldline's is currently trading at an EV/EBITDA 2016e of 8.8x (with the consolidation of Equens as of mid-May 2016 and including a possible loss of the French radar contract), i.e. an unjustified discount of 27% to payment processors evolving in the physical space. At our FV, the share would be at 12x, which is perfectly consistent with its positioning (a payment processor in the physical space).

In Video Games, 2016 should be buoyant for the French sector as a whole thanks to the speculation around Ubisoft and Gameloft. Only this theme will drive the share prices in 2016e. However and despite our buy ratings, we find it difficult to predict the exact timing of the likely takeover bids within the year (we expect a hostile or friendly offer on Gameloft and then a friendly one on Ubisoft). As a result, **we do not include any Video Game players in our Q1 2016 Top Pick list.**

In Semiconductors, our two best pick in the industry are ARM Holdings (Buy, FV 1,310p) and Infineon (Buy, FV EUR15). Amid a low visibility environment, we favour companies with solid profiles rather than value stocks. However, while we expect to see the end of inventory adjustment to gradually come over Q1 2016, we see no strong catalysts to trigger an outperformance of a particular semi stock. As a result, **we do not include any Semiconductor players in our Q1 Top Pick list.**

In Telecoms, the French market will be structured by the outcome of ongoing merger discussions between Orange and Bouygues Telecom. If the deal happens, all players on the market will benefit from it. If it does not, a hangover won't be far away. Promotional wars will go on, with no stabilisation to be expected soon. In all cases, high investments in 4G and fibre networks will remain crucial. On a European level, as in-country mergers are mostly behind us, we are seeing renewed interest in cross-border mergers and media telecom convergence. In particular, major players such as Vodafone, Deutsche Telekom, KPN or Telecom Italia might turn over a new page. **Since coverage is under construction, we do not provide any specific recommendation at this time.**

NEXT CATALYSTS

Software & IT Services: TCS' Q3 FY16 results on 12th January after the Indian markets close. Infosys' Q3 FY16 results on 14th January before the Indian markets open. IBM's FY15 results on 19th January after US markets close. FY15 sales and results for European companies starts on 22nd January (SAP).

Payments: Ingenico's FY earnings on 18th February (after trading), Worldline's FY earnings on 23rd February (after trading), Gemalto's FY earnings on 4th March (before trading) and Wirecard's FY earnings at the beginning of April.

Video Games: Gameloft's FY sales on 28th January (after trading) and Ubisoft's Q3 sales in February.

Semiconductors: Soitec's Q3 sales on 18th January (after trading). ASML's Q4 results on 20th January (before market opening). Infineon's Q1 results on 2nd February (before trading).

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