

Sage Group

Price 604.00p

H1 FY16 results slightly below our forecasts, FY16 outlook confirmed

Fair Value 550p (-9%)

SELL

Bloomberg	SGE L
Reuters	SGE.LN
12-month High / Low (p)	636.5 / 489.7
Market Cap (GBP)	6,519
Ev (BG Estimates) (GBP)	6,654
Avg. 6m daily volume (000)	2 823
3y EPS CAGR	8.9%

This morning Sage reported H1 FY16 results slightly below our estimates and consensus, while the outlook for FY16 (at least 6% lfl sales growth and organic operating margin of 27%) was reiterated. We expected an investment bias towards H1, but this appeared to be higher than we anticipated. The company is in line with its goal to generate GBP50m annualised costs savings. Following a 11% rise during the last 6 months, we expect the share price to react negatively short term.

ANALYSIS

- H1 FY16 results slightly below our forecasts.** For H1 FY16, Sage reported sales up 4.1% to GBP746.6m (+6.2% lfl), an organic operating profit of GBP189.3m or 25.4% of sales (vs. 26.4% for H1 FY15), an EBIT down 15.1% to GBP151.8m after GBP31m non-recurring costs, a net profit down 14.8% to GBP106.3m, and an adj. EPS down 1.5% to 12.09p (BG est.: 12.6p; consensus: 12.5p). Revenues are 2% above our GBP732.6m est. (+6.2% lfl) and the consensus' average (GBP730m, +6.2% lfl), but the organic operating profit is 2% our forecast (GBP193.5m or 26.4% of sales) and the consensus' average (GBP194m or 26.6%). Recurring revenues (69% of sales) were up 10% lfl - including subscriptions up 35.3% lfl, processing revenues (13%) were up 6.6% lfl, and SSRS (Software/software-related services, 18%) revenues were down 6.3% lfl. Free cash flow was down 13.9% to GBP142m, and underlying cash conversion was 111% (vs. 114% for H1 FY15). Finally, the interim ordinary dividend proposed for H1 FY16 is 4.8p per share (+8%).
- More details.** 1). Europe: sales +6.7% lfl to GBP398.1m (+9% in the UK, +7% in France, +6% in Germany, +6% in Spain, -4% on Rest of Europe), with Recurring up 8.8% lfl, Processing up 8.5% and SSRS down 0.9% lfl, for a 27.9% EBITA margin (vs. 27.8% in H1 FY15); 2). North America: sales +5.7% lfl to GBP255.6m, with Recurring up 9.4% lfl, Processing up 6% lfl and SSRS down 8.5% lfl, for an EBITA margin of 24.4% (vs. 24.7% in H1 FY15); 3). International: sales +5.4% lfl to GBP92.9m (+17% in Africa, +7% in Brazil, +7% in Australia, -29% in Middle East & Asia), with Recurring up 17.1% lfl, Processing up 12.2% and SSRS down 18.5% lfl, for an EBITA margin of 17% (vs. 24.7% in H1 FY15). Subscription contracts increased to 842,000 from 561,000. Sage X3 sales were up 17%, Sage One subscriptions increased to 230,000 from 115,000 one year ago (173,000 6 months ago), and Sage 50 Cloud supported subscriptions up 31% in Europe and up c. 100% in North America.
- Reiterated outlook, and investment in Fairsail.** The management remains confident in delivering for FY16 organic revenue growth of at least 6% with an organic operating margin of at least 27%. We forecast for FY16 sales up 6.3% lfl to GBP1,545m and an adj. EBITA margin of 27.1%. We expected an investment bias towards H1, but this appeared to be higher than we anticipated. The company is in line with its goal to generate GBP50m annualised costs savings, with GBP17m G&A savings related to people and facilities secured in H1, while the GBP31m non-recurring costs incurred in the first half essentially relate to G&A functions (GBP22m). It indicates business transformation will continue in H2, costing c. GBP100m. Finally, Sage announced an agreement to acquire a 20.7% stake in Fairsail, a provider of Human Capital Management (HCM) cloud-based solutions for SMBs, for GBP10m. Sage will offer Fairsail's cloud HCM products as an integrated solution for Sage X3, and intends to implement Fairsail as its global HCM solution.

	1 M	3 M	6 M	31/12/15
Absolute perf.	-4.1%	-0.6%	10.8%	0.1%
Softw. & Comp.	-2.6%	0.0%	-4.1%	-6.1%
DJ Stoxx 600	-0.8%	0.9%	-12.7%	-9.3%

YEnd Sept. (£m)	09/15	09/16e	09/17e	09/18e
Sales	1,436	1,545	1,672	1,793
% change		7.7%	8.2%	7.3%
EBITDA	418	450	490	532
EBIT	297.2	301.3	441.6	483.4
% change		1.4%	46.6%	9.5%
Net income	283.9	299.6	333.9	366.6
% change		5.5%	11.5%	9.8%

	09/15	09/16e	09/17e	09/18e
Operating margin	27.1	27.6	27.9	28.3
Net margin	13.5	13.3	18.6	19.2
ROE	22.5	22.5	29.2	27.8
ROCE	25.2	33.0	35.1	40.6
Gearing	39.6	14.7	-7.0	-24.8

(p)	09/15	09/16e	09/17e	09/18e
EPS	25.29	26.68	29.73	32.64
% change	-	5.5%	11.5%	9.8%
P/E	23.9x	22.6x	20.3x	18.5x
FCF yield (%)	4.3%	4.9%	5.4%	5.9%
Dividends (p)	13.10	13.76	14.44	15.16
Div yield (%)	2.2%	2.3%	2.4%	2.5%
EV/Sales	4.8x	4.3x	3.9x	3.5x
EV/EBITDA	16.4x	14.8x	13.2x	11.7x
EV/EBIT	17.6x	15.6x	13.8x	12.2x



VALUATION

- Sage's shares are trading at est. 15.6x FY16 and 13.8x FY17 EV/EBIT multiples.
- Net debt on 31st March 2016 was GBP404m (net gearing: 44%).

NEXT CATALYSTS

Analysts' meeting today at 8.45am BST / 9.45am CET / 3.45am EDT in London (London Stock Exchange, 10 Paternoster Square).

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