

Temenos Group

Price CHF53.80

Q2 2016 results above expectations, heading for the high-end of 2016 guidance

Fair Value CHF54 vs. CHF52 (0%)

NEUTRAL

Bloomberg	TEMN SW
Reuters	TEMN.SW
12-month High / Low (CHF)	57.6 / 31.9
Market Cap (CHF)	3,741
Ev (BG Estimates) (CHF)	3,876
Avg. 6m daily volume (000)	236.4
3y EPS CAGR	19.4%

We reiterate our Neutral recommendation, but have raised our DCF-derived Fair Value to CHF54 from CHF52 on recent CHF/USD fx rate moves. Yesterday evening Temenos reported Q2 2016 results above expectations. Management is now confident Temenos can reach the high-end of full-year guidance in view of deals recently signed in Wealth and Retail (BIL, Standard Chartered, Laurentian, BMO), while Brexit has no impact so far. We expect a positive share price reaction short-term.

ANALYSIS

- Q2 2016 results way above expectations.** On a non-IFRS basis, Q2 2016 sales were up 16.1% (+17% lfl) to USD153.8m, with total software licensing revenues up 24.9% lfl to USD60.4m (+30.9% lfl for licences, +6.7% lfl for SaaS and subscriptions), maintenance up 6.5% lfl, and services up 25.4% lfl following the number of software implementations gone live (24 vs. 13 in Q2 2015). Non-IFRS operating profit was up 22.3% to USD38.7m or 25.2% of sales (+1.3ppt), and non-IFRS EPS was up 16.7% to USD0.42. These figures were way above our forecasts (sales of USD139.8m, non-IFRS op. profit of USD33.4m or 23.9% of sales) and the consensus average (sales of USD142m, non-IFRS op. profit of USD35.6m or 25.1% of sales). Non-IFRS opex were up 17% lfl, while gross margin in services was down 3pp to 2.7%. On a LTM basis, operating cash conversion remained strong, at 130% of EBITDA (target >100%), with DSOs down 46 days (vs. a full-year target of 10-15 days).
- Other Q2 details.** 1) Q2 reflected excellent momentum - new wins stood at 21, up from 13 in Q2 2015 - with strong growth in almost all regions (est. +35% in Europe with strong growth in all segments and BIL as a key win, +25% in America with the signing of Laurentian Bank, and +60% in Asia with Standard Chartered Bank and Bank of Montreal, but an est. -42% in Middle East & Africa); 2) The win rate continued to increase, reaching close to 100% in Wealth with Standard Chartered Bank to deploy WealthSuite in 30+ countries, BIL in Europe, Bank of Montreal in Asia, and being strong in Retail with the two largest deals in the market won in H1 16; 3) The services gross margin was down 3pp due, as in Q1, to a lower share of "premium" services (18% vs. 24% in Q2 2015) as Temenos was involved in 'go live' implementations for some clients, and due to investments in project governance teams in order to ensure large deployments are successful.
- 2016 guidance: confidence for reaching the high-end.** On a non-IFRS basis, Temenos is now confident in reaching the high-end of 2016 guidance, i.e. revenues up 7.5-11% at cc, total software licensing up 10-15% at cc, and an operating margin of USD180-185m at cc (implying an operating margin up c. 2ppt to c. 30%). Adjusted for fx, this translates into total revenues of USD593-612m (vs. USD594-614m) and total software licensing of USD233-244m (vs. USD234-245m). Such optimism is driven by recent key wins - BIL and Standard Chartered Bank will start to generate revenues in Q3 - and "record levels" of revenue visibility for Q3 and the full-year. Since the Brexit referendum, all planned deals have closed with no delays or change in scope, and key accounts in the pipeline reconfirmed their need to invest in IT renovation. For Q3, including BIL and Standard Chartered and taking into account a cautious approach for H2, Temenos anticipates total software licensing up low single-digit (vs. a drop) against tough comps (Nordea). Finally, despite a decline over the last two quarters, it is confident it can deliver a gross margin in services for 2016 similar to that of 2015 (8.5%) as the governance team will ramp up over H2.

	1 M	3 M	6 M	31/12/15
Absolute perf.	-5.2%	4.6%	13.9%	3.6%
Softw. & Comp.	4.9%	3.5%	8.4%	0.9%
DJ Stoxx 600	0.9%	-2.8%	5.7%	-6.8%

YEnd Dec. (US\$m)	2015	2016e	2017e	2018e
Sales	542.5	615.1	677.6	747.1
% change		13.4%	10.2%	10.3%
EBITDA	212	248	278	309
EBIT	96.8	146.3	177.3	206.7
% change		51.2%	21.2%	16.6%
Net income	121.0	154.6	179.5	206.2
% change		27.8%	16.1%	14.9%

	2015	2016e	2017e	2018e
Operating margin	30.8	32.3	33.5	34.3
Net margin	12.2	17.7	20.0	21.7
ROE	17.7	24.0	24.4	22.6
ROCE	23.9	29.8	36.5	46.0
Gearing	71.2	30.2	-3.3	-33.3

(US\$)	2015	2016e	2017e	2018e
EPS	1.82	2.32	2.69	3.09
% change	-	27.8%	16.1%	14.9%
P/E	30.0x	23.5x	20.3x	17.6x
FCF yield (%)	4.4%	4.7%	5.4%	6.3%
Dividends (US\$)	0.45	0.50	0.55	0.60
Div yield (%)	0.8%	0.9%	1.0%	1.1%
EV/Sales	7.5x	6.4x	5.6x	4.8x
EV/EBITDA	19.1x	15.9x	13.6x	11.5x
EV/EBIT	24.3x	19.8x	16.6x	13.9x



VALUATION

- Temenos' shares are trading at est. 19.8x 2016 and 16.6x 2017 EV/EBIT multiples.
- Net debt on 30th June 2016 was USD288.4m (net gearing: 78%).

NEXT CATALYSTS

Q3 16 results on 19th October after markets close.

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