

## Indra Sistemas

Price EUR11.61

## Acquisition of Banco Popular's mortgage loan processing business

Fair Value EUR11 (-5%)

NEUTRAL

Bloomberg	IDR SM
Reuters	IDR.MC
12-month High / Low (EUR)	11.7 / 7.7
Market Cap (EURm)	1,906
Ev (BG Estimates) (EURm)	2,599
Avg. 6m daily volume (000)	862.6
3y EPS CAGR	

On Friday last week, Indra announced an exclusive agreement for the acquisition of the entity which runs Grupo Banco Popular's loan processing business, for an undisclosed sum. Adding 94 staff, the company doubles its mortgage loan BPO team. The deal, which is valid for 10 years, is assumed to be accretive to both EPS and free cash flow from 2016, given its high level of profitability. We estimate this acquisition is accretive by 2% to our adj. EPS ests. for 2016-18.

## ANALYSIS

- Rationale of the deal.** Indra has reached an exclusive agreement with Grupo Banco Popular for the complete management of its mortgage loan processing division for a 10-year period. This agreement will become effective on 31<sup>st</sup> October 2016, and involves the acquisition of the entity which runs this business. As such, 94 staff from Grupo Banco Popular will join Indra, which is doubling Indra's mortgage loan BPO team. The rationale of the deal for Banco Popular is to achieve segregation of duties on control and management functions for this business. At the same time, Indra increases its ability to offer proprietary technology solutions for the entire set of services across the mortgage loan business cycle, as well as improving its competitive position in international markets in this area.
- EPS and free cash flow accretion from 2016.** According to Indra, the deal offers a high level of profitability and is expected to be EPS and free cash flow accretive from 2016 onwards. The management also expects Banco Popular's mortgage loan management business generates significant synergies that improve Indra's margins in the same business, which essentially stems from the acquisition of BMB Gestión Documental between 2005 and 2007 and was seriously affected by the plummeting in the number of mortgage loans awarded in Spain from 2008. Since then, with the Spanish economy recovering, we understand Indra is looking to benefit from higher transaction volumes and related BPO revenues.
- Slightly increasing our forecasts.** If we assume that the acquired business generates c. EUR20m revenues per year and EBIT margin is around 20% (EBITDA margin: c. 45%), based on an acquisition price representing 6.5-7x EBITDA (i.e. c. EUR60-65m), we estimate EPS accretion to be 2% by 2017-18 including synergies with Indra's existing mortgage loan BPO business. We also estimate the deal increases free cash flow modestly, by c. EUR5-10m per year - the target set for 2018 is c. EUR200m and we estimate it for 2016 at EUR17m including non-recourse factoring. Finally, we estimate the acquired business will be accretive to our the non-IFRS operating margin by 0.1ppt and help Indra to achieve its goal of 10-11% for 2018 (BG est.: 10.2% vs. 10.1% previously).
- No change to our investment case.** The share price rose by 34% year-to-date following a sharp net debt reduction in Q4 2015, profitability improvement in line with the trajectory announced in July 2015 for 2018, and Q2 2016 results above consensus. While management remains cautious for the rest of the year due to the current political environment in Spain and Latin America and free cash flow remains low, we consider Indra is paving the way for future growth with strong order intake and Brazil starting to turn around.

	1 M	3 M	6 M	31/12/15
Absolute perf.	19.9%	17.8%	47.9%	33.9%
Softw. & Comp.	9.9%	10.6%	19.9%	4.7%
DJ Stoxx 600	2.9%	3.9%	10.8%	-5.4%

YEnd Dec. (€m)	2015	2016e	2017e	2018e
Sales	2,850	2,722	2,794	2,900
% change		-4.5%	2.6%	3.8%
EBITDA	107	223	308	370
EBIT	-641.0	160.0	237.0	295.0
% change		NS	48.1%	24.5%
Net income	-73.0	87.0	150.0	192.0
% change		NS	72.4%	28.0%

	2015	2016e	2017e	2018e
Operating margin	1.6	5.9	8.5	10.2
Net margin	-22.5	3.1	5.3	6.5
ROE	-208.1	21.5	27.3	26.0
ROCE	-11.7	11.7	17.7	21.9
Gearing	227.0	178.0	96.0	41.0

(€)	2015	2016e	2017e	2018e
EPS	-0.40	0.48	0.82	1.06
% change	-	NS	70.8%	29.3%
P/E	NS	24.2x	14.2x	11.0x
FCF yield (%)	NM	0.8%	8.4%	10.5%
Dividends (€)	0.00	0.00	0.00	0.00
Div yield (%)	NM	NM	NM	NM
EV/Sales	0.9x	1.0x	0.9x	0.8x
EV/EBITDA	24.3x	11.7x	7.9x	6.0x
EV/EBIT	56.6x	16.2x	10.2x	7.5x



## VALUATION

- Indra's shares are trading at est. 16.2x 2016 and 10.2x 2017 EV/EBIT multiples.
- Net debt on 30<sup>th</sup> June 2016 was EUR659.4m (net gearing: 199%).

## NEXT CATALYSTS

Q3 2016 results in November.

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SELL ratings 10,7%

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