

Sage Group

Price 737.00p

Pound story

Fair Value 690p vs. 600p (-6%)

SELL

Bloomberg	SGE L
Reuters	SGE.LN
12-month High / Low (p)	756.0 / 520.0
Market Cap (GBP)	7,959
Ev (BG Estimates) (GBP)	8,089
Avg. 6m daily volume (000)	2 666
3y EPS CAGR	13.3%

We reiterate our Sell rating, but increase our DCF-derived fair value to 690p from 600p on an upward revision of our adj. EPS ests. due to changes in our fx assumptions (+40p), and the roll-over of our DCF model to FY17 (+50p). Sage, which generates an est. 78% of its sales in foreign currencies, has benefited from the depreciation of the GBP since June. However, we consider a Neutral or a Buy rating could be justified only if the GBP drifts further, notwithstanding the fact we do not expect other catalysts short-term.

	1 M	3 M	6 M	31/12/15
Absolute perf.	1.7%	12.5%	17.8%	22.1%
Softw. & Comp.	0.1%	12.2%	13.3%	6.7%
DJ Stoxx 600	-1.5%	2.2%	2.2%	-7.0%

ANALYSIS

YEnd Sept. (£m)	09/15	09/16e	09/17e	09/18e
Sales	1,436	1,576	1,889	2,028
% change		9.8%	19.8%	7.3%
EBITDA	418	461	554	606
EBIT	297.2	314.7	503.9	555.9
% change		5.9%	60.1%	10.3%
Net income	286.7	310.6	383.5	423.6
% change		8.3%	23.5%	10.5%

	09/15	09/16e	09/17e	09/18e
Operating margin	27.1	27.8	28.1	28.7
Net margin	13.5	13.7	18.9	19.6
ROE	22.5	23.5	32.3	30.1
ROCE	25.2	33.8	42.5	49.9
Gearing	39.6	14.1	-15.8	-34.1

(p)	09/15	09/16e	09/17e	09/18e
EPS	25.59	27.57	33.86	37.23
% change	-	7.7%	22.8%	9.9%
P/E	28.8x	26.7x	21.8x	19.8x
FCF yield (%)	3.6%	4.2%	5.7%	5.5%
Dividends (p)	13.10	14.15	15.28	16.50
Div yield (%)	1.8%	1.9%	2.1%	2.2%
EV/Sales	5.8x	5.1x	4.1x	3.7x
EV/EBITDA	19.9x	17.5x	14.0x	12.4x
EV/EBIT	21.3x	18.5x	14.7x	12.9x

- Significant fx tailwinds since late July.** We increase our adj. EPS ests. by 1% for FY16 and 6% for FY17 and FY18 (FYE 30th September) given an update to our forward fx assumptions - which had not been changed since 27th July: 1.11 vs. 1.19 on GBP/EUR, 1.24 vs. 1.31 on GBP/USD, 17.1 vs. 19.0 on GBP/ZAR, 1.64 vs. 1.74 on GBP/CAD, 3.99 vs. 4.31 on GBP/BRL, and 1.63 vs. 1.74 on GBP/AUD. We estimate fx tailwinds to revenue growth at 3.5ppt (vs. 3.4ppt previously) for FY16 and an impressive 13.3ppt (vs. 7.3ppt previously) to FY17. We estimate that Sage generates 22% of its revenues in GBP while 78% is billed in foreign currencies (est. 31% in EUR, 30% in USD, 6% in ZAR, 5% in CAD, 3% in BRL, 3% in AUD).
- A Neutral or a Buy rating could be justified only if the British pounds drifts further.** We simulate that if the British pound depreciates further against other currencies and reaches a GBP/EUR rate of 1.00 – in that case we would obtain the following fx rates: GBP/USD of 1.12, GBP/ZAR of 15.4, GBP/CAD of 1.48, GBP/BRL of 3.59, and GBP/AUD of 1.47 -, fx tailwinds to revenue growth would rocket to 23.6ppt for FY17 our adj. EPS forecasts for FY17 and FY18 would have been raised by an additional 9% and our DCF-derived fair value would reach 760p – i.e. only in that case this could justify a Neutral rating on the stock. We deem that in order to justify a Buy rating, we need to assume the British pound falls to the point it reached a GBP/EUR rate of 0.90 – in that severe (and surely unlikely) case our DCF-derived fair value would reach 840p.
- No significant catalyst to expect until FY16 results.** Sage will report FY16 results on 30th November, and we do not expect any deviation from company guidance, which assumes revenues up at least 6% lfl (+6.1% year-to-date as of 30th June) and an organic operating margin of at least 27% vs. 27.5% in FY15 - this assumes a strong rebound in H2 above 28.5% from 25.4% reported for H1. We expect 6.3% lfl revenue growth for the year, which implies some acceleration in the September quarter, and the reaction of British SMBs to the Brexit is still uncertain. The GBP17m cost savings secured in H1 are in line with the GBP50m expected for FY16 (GBP33m expected for H2), which secures our 27.1% organic op. margin forecast for FY16. Finally, while it keeps reducing its net debt position over time, we consider that if Sage does not find any suitable acquisition target in the coming months, significant share buy-backs look unlikely due to the currently high share price level.

VALUATION

- Sage's shares are trading at est. 18.5x FY16, 14.7x FY17 and 12.9x FY18 EV/EBIT multiples.
- Net debt on 31st March 2016 was GBP270.9m (net gearing: 30%).

NEXT CATALYSTS

FY16 results on 30th November before markets open.

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