

Temenos Group

Price CHF66.10

Q3 2016 results above expectations; FY16 guidance raised, unsurprisingly

Fair Value CHF77 (+16%)

BUY

Bloomberg	TEMN.SW
Reuters	TEMN.SW
12-month High / Low (CHF)	68.2 / 41.9
Market Cap (CHF)	4,599
Ev (BG Estimates) (CHF)	4,709
Avg. 6m daily volume (000)	210.4
3y EPS CAGR	19.4%

Yesterday evening Temenos reported Q3 2016 results above expectations, thanks to an outstanding performance in Asia Pacific driven by several deals including Standard Chartered Bank. Unsurprisingly, management raised full-year guidance in view of the deal announced early October with the Bank of Ireland. With no impact from Brexit since core banking system renovation is strategic, and management is very confident in the pipeline, we expect a positive share price reaction short-term.

	1 M	3 M	6 M	31/12/15
Absolute perf.	8.4%	29.6%	24.7%	27.2%
Softw. & Comp.	-0.8%	9.7%	8.7%	6.4%
DJ Stoxx 600	0.7%	1.9%	-1.6%	-6.1%

ANALYSIS

- Q3 2016 results above expectations.** On a non-IFRS basis, Q3 2016 sales were up 8% (+10% lfl) to USD160.8m, with total software licensing revenues up 6% lfl to USD51.7m (+3.9% lfl for licences, +12.2% lfl for SaaS and subscriptions), maintenance up 11% lfl, and services up 21% lfl following the number of software implementations gone live (18 vs. 10 in Q3 2015). Non-IFRS operating profit was up 16.3% to USD50.8m or 31.6% of sales (+2.3ppt), and non-IFRS EPS was up 18% to USD0.59. These figures were above our forecasts (sales of USD153.4m, non-IFRS op. profit of USD47.5m or 31% of sales) and the consensus average (sales of USD154.5m, non-IFRS op. profit of USD48.5m or 31.4% of sales). Non-IFRS opex was up 7% lfl, while gross margin in services was up 3.9ppt to 9.6%. On a LTM basis, operating cash conversion remained very strong, at 125% of EBITDA (target >100%), with DSOs down 40 days (vs. a full-year target of 10-15 days) to 129.
- Other Q3 details.** 1) Total licensing revenue momentum was strongly positive in Asia Pacific (est. +225%) thanks to several deals including Standard Chartered Bank, followed by America (est. +11%), Middle East & Africa (est. -18%) and Europe (est. -29%, due to tough comps related to the Nordea deal); 2) New wins stood at 14, down from 19 in Q3 2015, but sales execution remained strong across all client tiers and segments; 3) the US pipeline is healthy and should lead to a growth acceleration in the coming quarter, yet Temenos still cannot mention the name of the US top 20 bank gone live in Q2 as a reference; 4) The services gross margin was up 3.9ppt thanks to a higher share of "premium" services (21% vs. 19% in Q3 2015); 5) DSOs are expected to decline further in Q4 vs. Q3, but probably not at the same extent as in Q4 2015 vs. Q3 (-15 days).
- 2016 guidance raised, as expected.** Given the Bank of Ireland deal, Temenos has raised FY16 guidance and now expects non-IFRS revenues up 12.5-14.5% at cc (vs. up 7.5-11% at cc), total software licensing up 15-20% at cc (vs. up 10-15% at cc), and an operating margin of USD184-186m at cc (vs. USD180-185m at cc) still implying an operating margin up c. 2ppt to c. 30%. Adjusted for fx, this translates into total revenues of USD621-632m (vs. USD593-612m) and total software licensing of USD245-256m (vs. USD233-244m). Management considers revenue visibility is at a record level – driven by Bank of Ireland, for which we consider licence revenues for Q4 2016 are around USD12m -, the sales pipeline for 2017 is very strong in all geographies and segments, and no slowdown in decision making has been seen since the Brexit referendum. Finally, it is confident it can deliver a gross margin in services for 2016 similar to that of 2015 (8.5%) as the governance team ramps up over H2.

YEnd Dec. (US\$m)	2015	2016e	2017e	2018e
Sales	542.5	629.2	689.0	762.2
% change		16.0%	9.5%	10.6%
EBITDA	212	259	286	321
EBIT	96.8	152.6	182.0	214.8
% change		57.7%	19.3%	18.0%
Net income	121.0	162.9	185.4	215.1
% change		34.6%	13.8%	16.0%

	2015	2016e	2017e	2018e
Operating margin	30.8	33.3	34.1	35.1
Net margin	12.2	18.3	20.4	22.3
ROE	17.7	25.1	24.8	23.1
ROCE	23.9	32.9	40.1	52.0
Gearing	71.2	24.1	-9.6	-39.4

(US\$)	2015	2016e	2017e	2018e
EPS	1.82	2.34	2.66	3.09
% change	-	29.0%	13.8%	16.0%
P/E	36.8x	28.5x	25.1x	21.6x
FCF yield (%)	3.6%	4.3%	4.6%	5.4%
Dividends (US\$)	0.45	0.50	0.55	0.60
Div yield (%)	0.7%	0.7%	0.8%	0.9%
EV/Sales	9.1x	7.6x	6.7x	5.7x
EV/EBITDA	23.2x	18.4x	16.1x	13.6x
EV/EBIT	29.5x	22.7x	19.5x	16.3x



VALUATION

- Temenos' shares are trading at est. 22.7x 2016 and 19.5x 2017 EV/EBIT multiples.
- Net debt on 30th September 2016 was USD273.1m (net gearing: 67%).

NEXT CATALYSTS

FY16 results on 14th February 2017 after markets close.

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