

ELMO SOFTWARE LTD

HOLD

Executing well across growth opportunity but trading at full valuation

Software & Services / Application Software

13 February 2020

COMPANY UPDATE

Ticker	ELO
Stock Price	\$7.70
Target Price	\$7.72
Forecast Capital Return	0.3%
Forecast Dividend Yield	0.0%
Estimated Total Return - 12 Mth Forward	0.3%

Company market data

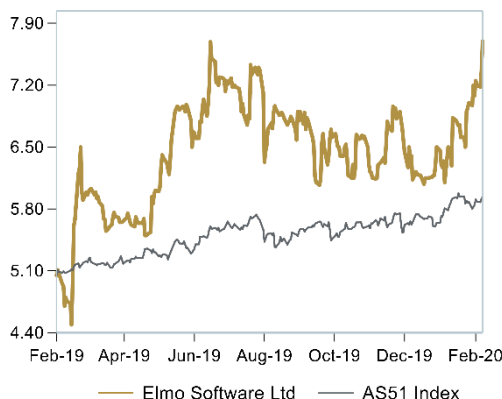
Market Cap.	\$587.9m
Free Float (%)	70.0
Enterprise Value	\$516.4m
52 Week Range	\$4.49 - \$7.70
Shares Out.	76.4m
Avg. Daily Value	\$0.6m

Estimates changes	2019a	2020e	2021e	2022e
Core NPAT - <i>old</i>	(13.3)	(13.7)	(11.8)	(8.5)
Core NPAT - <i>new</i>	(13.3)	(15.7)	(15.7)	(13.6)
% Change	0.0	14.8	32.8	60.6
Core EPS dil. (€) - <i>old</i>	(20.6)	(18.7)	(15.5)	(11.1)
Core EPS dil. (€) - <i>new</i>	(20.6)	(21.4)	(20.6)	(17.8)
% Change	0.0	14.8	32.7	60.3
DPS (€) - <i>old</i>	0.0	0.0	0.0	0.0
DPS (€) - <i>new</i>	0.0	0.0	0.0	0.0
% Change	-	-	-	-

All figures are in AUD unless otherwise specified.

Share price performance

Elmo Software Ltd vs. AS51 (rebased index)



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EVENT

ELMO has reported its 1H20 results which were in line with expectations given ARR of \$52m (+42.9% yoy) & Revenue of \$23.6m (+30.3%) were pre-reported. EBITDA losses widened to -\$2.6m (1H19: -\$1.9m) with NPAT of -\$8.5m (+6.7% vs MOEe: -\$9.1m).

Key operational metrics demonstrated strong execution across cross-selling into existing customers and selling the wider integrated, modular platform into new customers.

- ARPU \$35.2k (+9.1% yoy)
- Customer revenue retention at 110%
- Average modules per customer of 2.6 vs 2.2 at Dec-18
- Average incoming modules per new customer at 3.9 vs 3.7 in 2H19

Acquisition of Vocam, HR & safety video e-learning content provider for \$3.5m consideration, based on \$1.5m revenue (2.3x EV/sales) and EBITDA neutral.

Guidance has been updated to include Vocam, with organic guidance unchanged. FY20 guidance now sits at ARR of \$62.5m to \$64.5m, Revenue of \$53.3m to \$55.3m and EBITDA of -\$1.0m to -\$3.0m.

IMPACT

We raise our FY20/FY21/FY22 revenue estimates by 0.4%/2.8%/2.0% to \$54.0m/\$71.4m/\$89.6m which primarily reflects the impact of the Vocam acquisition.

We also increase our EV/FY21e Sales multiple valuation to 7.0x from 6.5x which reflects a re-rating in peer multiples.

Our target price increases to \$7.72 (prev: \$7.42) as a result of the changes.

INVESTMENT VIEW

We believe ELMO is executing well through cross-selling into existing customers and selling the wider platform into new customers. While we like the ELMO story and believe there is a strong opportunity for the company to capitalise on its positioning as a cloud-based HR & Payroll software platform in the mid-market, ELMO is trading close to our fair value estimate at 7.2x EV/FY21e Sales given that FY21e organic revenue growth of 32% is being generated with an effective free cash flow margin of -30%.

Maintain Hold, \$7.72 target price.

Y/E Jun 30	2019a	2020e	2021e	2022e
EBITDA	(2.6)	(2.7)	1.9	8.4
EV/EBITDA	nm	nm	274.6x	61.4x
Core NPAT	(13.3)	(15.7)	(15.7)	(13.6)
Core EPS (Diluted) (€)	(20.6)	(21.4)	(20.6)	(17.8)
P/E	nm	nm	nm	nm
EPS growth	(89.6%)	3.9%	(4.1%)	(13.6%)
DPS (€)	0.0	0.0	0.0	0.0
Yield	0.0%	0.0%	0.0%	0.0%
DPS growth	-	-	-	-
Dividend Payout Ratio	0.0%	0.0%	0.0%	0.0%

All figures are in AUD.

RESULTS SUMMARY

Given ELMO had pre-reported revenue, our focus was on the costs which were in line with expectations with 1H20 NPAT of -\$8.5m, +6.7% vs our estimate of -\$9.1m, which primarily reflected a one-off \$1.0m tax benefit. The key difference in reported EBITDA of -\$2.6m versus our estimate of -\$4.2m reflected the impact of AASB16.

Figure 1: Financials vs PCP & Moelis Estimates

Type	Actual	Actual		MOE est	
Year End Jun	1H19	1H20	Change	1H20	Diff
Revenue	17.7	23.6	33.8%	23.6	0.1%
Cost of Sales	(2.6)	(3.6)	38.2%	(3.4)	6.3%
Gross Profit	15.0	20.0	33.1%	20.2	(0.9%)
<i>Margin</i>	85.1%	84.6%	(0.5ppts)	85.5%	+0.9ppts
Other income	0.1	0.0	(81.3%)	-	nm
Opex	(17.0)	(22.6)	32.7%	(24.4)	(7.1%)
EBITDA	(1.9)	(2.6)	35.6%	(4.2)	(37.6%)
<i>Margin</i>	(10.9%)	(11.1%)	(0.1ppts)	(17.7%)	(6.7ppts)
D&A	(4.3)	(6.9)	58.1%	(5.0)	37.4%
EBIT	(6.3)	(9.5)	51.2%	(9.2)	3.3%
Interest	0.1	0.0	(65.9%)	0.1	(64.0%)
Tax	(1.0)	1.0	(195.9%)	-	nm
NPAT (underlying)	(7.2)	(8.5)	18.2%	(9.1)	(6.7%)

Source: Company, Moelis Analysis

Overall, the result reflected strong execution across cross-selling into existing customers and selling the wider integrated, modular platform into new customers.

Headcount investment remains strong with 91 net new FTEs added during 1H20, with investment expected to remain strong, albeit at reduced levels in 2H20.

Customer churn ticked up to 7.1% from 6.4%, although remains at attractive levels.

Figure 2: KPIs

Year End Jun	1H19	1H20	Change
Customers	1,129	1,478	30.9%
ARR	36.4	52.0	42.9%
ARPU	32.2	35.2	9.1%
Customer retention (LTM)	93.6%	92.9%	(0.7ppts)
Net revenue retention (LTM)	n/a	110.7%	n/a
Ave. Modules Per Customer	2.2	2.6	18.2%
Ave. Modules Per Incoming	3.7	3.9	5.4%
Employees	221	368	66.5%

Source: Company, Moelis Analysis

Guidance has been updated to reflect the impact of the Vocam acquisitions, with organic guidance reaffirmed.

Figure 3: FY20 Guidance

FY20 guidance organic		Contribution from Vocam		FY20 upgraded guidance
ARR \$61 - 63m	+	ARR \$1.5m	=	ARR \$62.5 - 64.5m
Revenue \$53 - 55m	+	Revenue \$0.3m	=	Revenue \$53.3 - 55.3m
EBITDA (\$1 - 3m)	+	EBITDA -	=	EBITDA ¹ (\$1 - 3m)

Source: Company releases

CHANGES TO VALUATION

Valuation Methodology

Our valuation methodology for ELMO uses an equally weighted DCF and peer EV/Sales multiple valuation. We roll forward our blended valuation 12 months by the cost of equity to derive a target price.

Blended Valuation Assumptions:

- **DCF (\$6.53 valuation):** Our DCF uses a WACC of 10.3% and a terminal value EV/EBITDA of 15.0x in FY25.
- **Peer EV/Sales Multiple Valuation (\$7.49 valuation):** Our Peer EV/Sales Multiple Valuation uses 7.0x EV/FY21 Sales, derived using comparable domestic peer multiples.

Elmo Software Ltd (ELO)

Market Cap: \$588m

Last Price: \$7.70

Target Price: \$7.72

Hold

Y/E Jun 30

Profit and Loss (\$m)	2018a	2019a	2020e	2021e	2022e
Revenue	26.5	40.1	54.0	71.4	89.6
<i>Growth</i>	60.1%	51.0%	34.8%	32.3%	25.4%
EBITDA	1.3	(2.6)	(2.7)	1.9	8.4
<i>Growth</i>	24.3%	(295.6%)	4.5%	(169.4%)	347.1%
Dep'n & Amort	(4.4)	(9.4)	(14.4)	(17.9)	(22.0)
EBIT	(3.1)	(12.0)	(17.1)	(16.1)	(13.6)
<i>Growth</i>	124.9%	286.8%	42.3%	(6.2%)	(15.6%)
Net Interest Expense	0.3	0.1	0.4	0.3	(0.1)
Profit Before Tax	(2.8)	(11.9)	(16.7)	(15.7)	(13.6)
Tax	0.0	(1.4)	1.0	0.0	0.0
<i>Tax Rate (%)</i>	(0.5%)	(11.5%)	5.7%	0.0%	0.0%
Minorities	0.0	0.0	0.0	0.0	0.0
NPAT (Underlying)	(2.9)	(13.3)	(15.7)	(15.7)	(13.6)
<i>Growth</i>	106.9%	365.4%	18.1%	(0.1%)	(13.3%)
One-Off Items	0.0	0.0	0.0	0.0	0.0
NPAT (Reported)	(2.9)	(13.3)	(15.7)	(15.7)	(13.6)
EPS (Underlying) (€)	(198.8)	(20.6)	(21.4)	(20.6)	(17.8)
<i>Growth</i>	-	(89.6%)	3.9%	(4.1%)	(13.6%)

Balance Sheet (\$m)	2018a	2019a	2020e	2021e	2022e
Cash	46.0	27.7	63.0	39.4	24.0
Inventory	0.0	0.0	0.0	0.0	0.0
Current Receivables	6.5	9.5	12.1	15.2	18.9
PPE	5.8	4.2	5.2	5.6	6.0
Intangibles	35.8	67.3	77.1	86.5	95.5
Other	5.3	0.7	1.4	1.4	1.4
Total Assets	99.3	109.5	158.8	148.0	145.9
Current Payables	4.6	7.3	9.7	12.1	15.2
ST Debt	0.0	0.0	0.0	0.0	0.0
LT Debt	0.8	0.0	0.0	0.0	0.0
Provisions	13.9	20.1	23.2	29.0	35.4
Other	11.8	26.8	19.6	14.6	14.6
Total Liabilities	31.1	54.1	52.5	55.8	65.2
Net Assets	68.2	55.4	106.2	92.3	80.7
Equity & Reserves	72.5	73.6	140.1	141.9	143.9
Retained Profits	(4.3)	(18.2)	(33.9)	(49.6)	(63.2)
Shareholders' Equity	68.2	55.4	106.2	92.3	80.7
Minorities	0.0	0.0	0.0	0.0	0.0
Total Equity	68.2	55.4	106.2	92.3	80.7

Cashflow (\$m)	2018a	2019a	2020e	2021e	2022e
EBITDA	1.3	(2.6)	(2.7)	1.9	8.4
Net Interest	0.0	0.9	0.3	0.3	(0.1)
Tax	0.0	(1.4)	1.0	0.0	0.0
Δ in Working Capital	0.0	5.7	2.8	5.2	5.6
Other	0.0	3.0	(2.4)	0.0	0.0
Operating Cash Flow	1.3	5.6	(1.0)	7.4	14.0
<i>Growth</i>	24.3%	322.9%	(118.0%)	(836.9%)	88.2%
Capex	(10.5)	(10.4)	(21.0)	(25.5)	(29.1)
Acquisitions	(17.6)	(13.7)	(7.8)	(5.0)	0.0
Divestments	0.0	0.0	0.0	0.0	0.0
Other	0.3	2.9	(1.6)	0.0	0.0
Investing Cash Flow	(27.8)	(21.3)	(30.4)	(30.5)	(29.1)
Equity Raised	43.0	(0.1)	67.8	0.0	0.0
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Net Borrowings	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	(1.8)	0.0	0.0
Financing Cash Flow	43.0	(0.1)	66.0	0.0	0.0
FX / Non Cash Items	0.0	0.0	0.0	0.0	0.0
Change in Cash	16.6	(15.7)	34.6	(23.1)	(15.1)
Free Cash Flow	(9.1)	(4.8)	(22.1)	(18.1)	(15.1)

Valuation Summary	
Current Mkt Capitalisation	587.9
Shares on Issue	76.4
Last Price	7.70
12 Mth Target Price	7.72
Total Estimated 12 Mth Return	0.3%
12 Mth Fwd Capital Return	0.3%
12 Mth Fwd Dividend Yield	0.0%

Valuation Ratios	2018a	2019a	2020e	2021e	2022e
EPS (Underlying) (€)	(198.8)	(20.6)	(21.4)	(20.6)	(17.8)
<i>Growth</i>	-	(89.6%)	3.9%	(4.1%)	(13.6%)
P/E (x)	nm	nm	nm	nm	nm
Small Industrials (ex Fin's)	0.0x	0.0x	0.0x	0.0x	0.0x
Premium / (Discount)	nm	nm	nm	nm	nm
EV/EBITDA (x)	389.4x	nm	nm	274.6x	61.4x
Small Industrials (ex Fin's)	0.0x	0.0x	0.0x	0.0x	0.0x
Premium / (Discount)	nm	nm	nm	nm	nm
DPS (€)	0.0	0.0	0.0	0.0	0.0
<i>Growth</i>	-	-	-	-	-
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	100.0%	100.0%	100.0%	100.0%	100.0%
NTA	54.0	24.1	65.3	41.9	21.3
NTA/Share (\$)	37.54	0.37	0.89	0.55	0.28

Performance Ratios	2018a	2019a	2020e	2021e	2022e
ROA	(3.0%)	(12.1%)	(9.9%)	(10.6%)	(9.3%)
ROE	(4.4%)	(24.0%)	(14.8%)	(17.0%)	(16.9%)
ROIC	(31.9%)	(41.9%)	(45.5%)	(33.4%)	(24.8%)
Net Debt (Cash) (\$m)	(45.2)	(27.7)	(63.0)	(39.4)	(24.0)
Net Debt/EBITDA (x)	0.0x	0.0x	0.0x	0.0x	0.0x
ND/(ND + Equity) (%)	(196.3%)	(100.0%)	(145.9%)	(74.5%)	(42.4%)
Interest Cover (x)	(12.2x)	(129.0x)	(39.4x)	(46.4x)	206.2x
Working Capital	(14.8)	(28.4)	(25.2)	(25.4)	(31.0)
Working Capital/Sales (%)	(55.6%)	(70.9%)	(46.7%)	(35.6%)	(34.6%)

Cash Flow Metrics	2018a	2019a	2020e	2021e	2022e
FCF/Share (\$)	0.00	(0.08)	(0.31)	(0.24)	(0.20)
Price/FCPS (x)	-	nm	nm	nm	nm
Free Cash Flow Yield (%)	0.0%	(1.0%)	(4.0%)	(3.1%)	(2.6%)
Gross Cash Conversion	344.7%	(265.4%)	(71.4%)	529.7%	199.5%
Capex/Sales (%)	(39.5%)	(26.1%)	(39.0%)	(35.7%)	(32.5%)
Capex/Depreciation (x)	0.0x	0.0x	0.0x	0.0x	0.0x

Margins	2018a	2019a	2020e	2021e	2022e
EBITDA	5.0%	(6.5%)	(5.0%)	2.6%	9.4%
EBIT	(11.7%)	(30.0%)	(31.7%)	(22.5%)	(15.1%)
NPAT	(10.8%)	(33.2%)	(29.1%)	(22.0%)	(15.2%)

Valuation Methodology	
WACC (%)	10.3%
Discounted Cash Flow Valuation	6.53
Sum-of-the-Parts Valuation	7.49
Average Valuation	7.01
12 Mth Target Price	7.72

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Rating and Price Target History: Elmo Software Ltd (ELO) as of 12/02/2020



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